92-87

No. _____

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

In re:

KOREAG, CONTROLE ET REVISION, S.A. as Official Liquidator of MEBCO BANK, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

KOREAG, CONTROLE et REVISION, S.A.,

Petitioner,

—v.—

REFCO F/X ASSOCIATES, INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether, under Section 304(b) of the Bankruptcy Code, a bankruptcy court, before it can turn over property to a foreign representative for administration in the foreign insolvency proceeding, must make a threshold determination that an American creditor is not entitled to the property under local law despite the fact that the factors set forth in § 304(c) for affording ancillary relief have all been satisfied.

2. Whether, if such a threshold determination is necessary, the foreign law, rather than state law, determines whether the American creditor is entitled to the property.

PARTIES TO THE PROCEEDING

The parties to the proceedings in the court below were: the Official Liquidator of Mebco Bank, S.A., now called ATAG Ernst & Young Ltd., and Refco F/X Associates, Inc. The following companies are parent companies of ATAG Ernst & Young Ltd:

a) ATAG Ernst & Young Holding Ltd.

b) Stiftung ATAG Treuhand

There are no subsidiary companies.

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PETITION FOR A WRIT OF CERTIORARI

The Official Liquidator of Mebco Bank, S.A., now called ATAG, Ernst & Young Ltd., respectfully petitions for a writ of certiorari to review the decision of the United States Court of Appeals for the Second Circuit in this case.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Second Circuit (App. 1a-40a) is reported at 961 F.2d 341. The orders of the United States District Court for the Southern District of New York affirming the judgment of the bankruptcy court (App. 69a-74a) are unreported. The opinion of the United States Bankruptcy Court for the Southern District of New York (App. 48a-66a) is reported at 130 B.R. 705.

JURISDICTION

The court of appeals entered its decision on April 9, 1992. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1) (1988).

STATUTES INVOLVED

Section 101(23) and (24) of the Bankruptcy Code, 11 U.S.C. § 101 (23) and (24) (Supp. 1992), provide:

> (23) "foreign proceeding" means proceeding, whether judicial or administrative and whether or not under bankruptcy law, in a foreign country in which the debtor's domicile, residence, principal place of business, or principal assets were located at the commencement of such proceeding, for the purpose of liquidating an estate, adjusting debts by composition, extension, or discharge, or effecting a reorganization;
>
> (24) "foreign representative" means duly selected trustee, administrator, or other representative of an estate in a foreign proceeding.

Section 304 of the Bankruptcy Code, 11 U.S.C. § 304 (1987), provides:

(a) A case ancillary to a foreign proceeding is commenced by the filing with the bankruptcy court of a petition under this section by a foreign representative.

(b) Subject to the provisions of subsection (c) of this section, if a party in interest does not timely controvert the petition, or after trial, the court may—

(1) enjoin the commencement or continuation of—

(A) Any action against—

(i) a debtor with respect to property involved in such foreign proceeding; or

(ii) such property; or

(B) the enforcement of any judgment against the debtor with respect to such property, or any act or the commencement or continuation of any judicial proceeding to create or enforce a lien against the property of such estate;

(2) order turnover of the property of such estate, or the proceeds of such property, to such foreign representative; or

(3) order other appropriate relief.

(c) In determining whether to grant relief under subsection (b) of this section, the court shall be guided by what will best assure an economical and expeditious administration of such estate, consistent with—

(1) just treatment of all holders of claims against or interests in such estate;

(2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;

(3) prevention of preferential or fraudulent dispositions of property of such estate;

(4) distribution of proceeds of such estate substantially in accordance with the order prescribed by this title;

(5) comity; and

(6) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

Section 306 of the Bankruptcy Code, 11 U.S.C. § 306 (1987), provides:

> An appearance in a bankruptcy court by a foreign representative in connection with a petition or request under section 303, 304, or 305 of this title does not submit such foreign representative to the jurisdiction of any court in the United States for any other purpose, but the bankruptcy court may condition any order under section 303, 304, or 305 of this title on compliance by such foreign representative with the orders of such bankruptcy court.

Section 365(a) of the Bankruptcy Code, 11 U.S.C. § 365(a) (Supp. 1992), provides:

> Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.

Section 541 of the Bankruptcy Code, 11 U.S.C. § 541 (1987 & Supp. I 1992), provides in pertinent part:

> (a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
>
> (1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is—

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date—

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

Section 544 of the Bankruptcy Code, 11 U.S.C. § 544 (1987 & Supp. I 1992), provides:

> (a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by-
>
> (1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;
>
> (2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or
>
> (3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.
>
> (b) The trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

Section 546(c) of the Bankruptcy Code, 11 U.S.C. § 546(c) (Supp. 1992), provides:

> Except as provided in subsection (d) of this section, the rights and powers of a trustee under sections 544(a), 545, 547, and 549 of this title are subject to any statutory or common-law right of a seller of goods that has sold goods to the debtor, in the ordinary course of such seller's business, to reclaim such goods if the debtor has received such goods while insolvent, but—
>
> (1) such a seller may not reclaim any such goods unless such seller demands in writing reclamation of such goods before ten days after receipt of such goods by the debtor; and
>
> (2) the court may deny reclamation to a seller with such a right of reclamation that has made such a demand only if the court—
>
> (A) grants the claim of such a seller priority as a claim of a kind specified in section 503(b) of this title; or
>
> (B) secures such claim by a lien.

STATEMENT OF THE CASE

On April 27, 1989, the Federal Banking Commission of Switzerland, acting pursuant to Swiss law, placed Mebco Bank, S.A. ("Mebco"), a Swiss corporation with its principal place of business in Geneva, in liquidation. Later that day, the Banking Commission appointed Koreag, Controle et Revision S.A. ("Koreag" or the "Liquidator") as Mebco's Official Liquidator. The Liquidator is charged with the responsibility of distributing Mebco's assets equitably among Mebco's more than 400 creditors worldwide. Thus, since April 27, 1989, Mebco has been the subject of a "foreign proceeding" within the meaning of 11 U.S.C. § 101(23) and 11 U.S.C. § 304 with the Liquidator as its "foreign representative" within the meaning of 11 U.S.C. § 101(24) and 11 U.S.C. § 304.

On May 5, 1989, after learning of the Swiss insolvency proceedings, Refco F/X Associates, Inc. ("Refco") commenced a breach of contract action against Mebco in the United States District Court for the Southern District of New York, asserting that Mebco had failed to perform its side of currency exchange agreements that had been performed by Refco after the public announcement of Mebco's liquidation. The same day, Refco obtained an *ex parte* order of attachment against Mebco's bank account at Swiss Bank Corporation's New York branch ("Swiss Bank-N.Y."). Refco is a New York corporation engaged in the business of international commodity and currency transactions, and is the subsidiary of a diversified $2 billion company which is also engaged in international financial transactions.

Between June 1988 and April 1989, Refco's London office engaged in currency transactions with Mebco on a daily basis, sometimes conducting as many as five transactions in a single day. While these currency exchange agreements obviously required the use of bank accounts throughout the world, Refco and Mebco dealt with each other *only* through their respective offices in London and Geneva. Indeed, although Mebco maintained the Swiss Bank-N.Y. account to facilitate the payment and receipt of United States currency, Mebco was neither authorized to do business nor present in New York. At the time Refco obtained the *ex parte* attachment, the Swiss Bank-N.Y. account held over $12.5 million, $6.9 million of which had been paid in by Refco pursuant to various exchange agreements and $5.6 million of which had been paid in by others.

The Liquidator opposed confirmation of the attachment. It argued that comity should be afforded to the Swiss liquidation proceedings and requested that the funds held in the account be turned over to it for administration in Switzerland. On December 11, 1989, the district court found that § 304 of the Bankruptcy Code was the "preferred remedy" and directed the Liquidator to make its application to the bankruptcy court (App. 46a-47a). Section 304 authorizes the commencement by a foreign representative of a case ancillary

to a foreign proceeding in which the American bankruptcy court may order, *inter alia*, turnover of certain property to the foreign representative.

On January 5, 1990, the Liquidator filed a petition pursuant to § 304. The Liquidator sought an order enjoining the continuation of Refco's action in the district court; enjoining the commencement of any further actions against Mebco or its property within the Southern District of New York; and directing that the funds held in the account be turned over to the Liquidator for administration in Switzerland.

On April 25, 1990, the bankruptcy court issued an order granting the Liquidator's motion for a preliminary injunction. On August 23, 1991, the bankruptcy court issued an opinion holding that the Liquidator satisfied the requirements of § 304, (App. 48a-66a), and on September 4, 1991, the bankruptcy court issued an order granting summary judgment to the Liquidator (App. 67a-68a).

The bankruptcy court rejected Refco's argument that its alleged state-law remedies of reclamation and constructive trust deprived the court of subject matter jurisdiction to adjudicate the § 304 petition, emphasizing that whenever a local creditor is forced to have its claim determined in a foreign forum, it stands to lose rights provided by local law. The bankruptcy court explained that Refco's position placed the "cart before the horse"; it rested on the "underlying assumptions . . . that the petitioner's turnover request will be denied, Refco will not be forced to participate in the Swiss liquidation proceedings and that Refco's claim will be adjudicated in an American court." The bankruptcy court concluded that it had jurisdiction to hear the § 304 petition by virtue of the Liquidator's undisputed allegation that under Swiss law the Swiss Bank-N.Y. account is considered Mebco's property and is part of the property involved in the Swiss proceedings (App. 56a-57a).

The bankruptcy court then considered the criteria set forth in § 304(c) and concluded that each of the relevant § 304(c)

factors weighed in favor of granting the petition. Specifically, the bankruptcy court found that:

— Refco's claim would receive just treatment in Switzerland because Swiss law does not discriminate against non-Swiss creditors, § 304(c)(1);

— Refco would not be prejudiced or inconvenienced if forced to adjudicate its claim in Switzerland because it is a sophisticated creditor with substantial assets and European offices which assumed the risk of a foreign bankruptcy when it decided to enter into an ongoing business relationship with a Swiss bank, § 304(c)(2);

— Swiss law provides for setting aside preferential or fraudulent dispositions, § 304(c)(3);

— Switzerland's insolvency procedures are "fundamentally fair" and "substantially similar" to the United States Bankruptcy Code, § 304(c)(4); and

— "comity" requires deferring to the Swiss insolvency proceedings because they comport with due process and because the best way to insure an equitable distribution of a foreign debtor's assets is in a single proceeding which determines the rights of all creditors, § 304(c)(5).

(App. 57a-65a). Having found that each of the relevant § 304(c) factors weighed in favor of ancillary relief, the bankruptcy court concluded that turnover of the funds in the Swiss Bank–N.Y. account for administration in Switzerland would "best assure [the] economical and expeditious administration" of Mebco's estate that § 304(c) requires (App. 53a-54a, 64a-65a).

Refco appealed, and on September 13, 1991, the district court entered an order, revised on September 16, 1991, summarily affirming the bankruptcy court's order (App. 69a-71a).

On April 9, 1992, the Court of Appeals for the Second Circuit vacated the district court's order and remanded for further proceedings. The Second Circuit acknowledged that the bankruptcy court had not abused its discretion in finding the § 304(c) factors were satisfied. The court of appeals nevertheless reversed the turnover order, holding that a "threshold determination" concerning the ownership of the property must be made under local law before property may be turned over to a foreign representative under § 304. The court of appeals rested its conclusion on its reading of the phrase "turnover of the property of such estate" in § 304(b)(2). The Second Circuit held that "property of *such* estate" in § 304(b)(2) has the same meaning as "property of *the* estate" for purposes of 11 U.S.C. § 541 (emphasis added). Consequently, under the Second Circuit's reading of § 304, if a particular asset would not be part of a domestic debtor's estate, it is not subject to turnover under § 304(b)(2), even though it is part of the property being administered in the foreign forum. The court of appeals remanded the case for findings as to whether the funds in the account were "owned" by Refco under local law (App. 1a-42a).

The ruling below eviscerates § 304. It bars the turnover of assets which are unquestionably part of the property being administered in a foreign insolvency proceeding, even though the foreign proceedings comport with our notions of due process, and even though the factors set forth in § 304(c) call for ancillary relief. The net effect is to require a preliminary hearing on the merits of a creditor's claim under local law before turnover may be ordered in an ancillary case. The Second Circuit's opinion is at war with the language of § 304 and the doctrine of international comity upon which it is based. To protect an American creditor from turnover, the Second Circuit destroyed the statute. Because the opinion is likely to have far reaching effects on transnational bankruptcies in general and on the liquidation of Mebco in particular, the Liquidator has filed this petition for a writ of certiorari.

REASONS FOR GRANTING THE WRIT

The correct interpretation of § 304 of the Bankruptcy Code is key to the proper administration of the rising tide of transnational bankruptcies. By requiring bankruptcy courts to make a threshold adjudication of how a creditor's claim would fare under state property law before determining which forum should administer the bankruptcy, the Second Circuit violated Congress's stated desire in § 304(c) to "assure an economical and expeditious administration" of a foreign debtor's estate. In reaching that result, the Second Circuit erroneously substituted local law for the law of the foreign tribunal; used the definition of "estate" under § 541 of the Bankruptcy Code when Congress intended in § 304 that foreign concepts apply; and greatly complicated efforts of foreign representatives to marshal assets in a single forum that would fairly consider the rights of *all* creditors. The decision below rewards fast-moving domestic creditors like Refco who successfully attach the assets of a foreign debtor and penalizes creditors who wait their turn for relief in the foreign insolvency proceeding. An early and definitive resolution of this important issue of federal statutory interpretation is critical to protect the integrity of the many transnational bankruptcies which will be governed by the Second Circuit's decision.[1]

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1 The number of § 304 petitions filed annually has been increasing at a fairly steady pace. According to statistics kept by the Administrative Office of the United States Courts, only fifteen § 304 petitions were filed nationwide between 1981 and 1986 as compared to eighty-one between 1987 and 1992. Not surprisingly, given the presence of New York City within the Second Circuit, a significant percentage of § 304 cases filed to date have been in the Second Circuit. In 1992, 61% of all § 304 petitions were filed within the Second Circuit; in 1991, 80%; in 1990, 54%; in 1989, 47% and in 1988, 40%. This trend obviously makes the development of a conflict in the circuits less probable. It also means that the Second Circuit's ruling, if left unreviewed, will have a substantial impact on the future use of § 304.

1. The Decision Below Is Contrary to the Plain Language and Underlying Policy of § 304

Comity is the name given to the "recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws." *Hilton* v. *Guyot*, 159 U.S. 113, 164 (1895). Over one hundred years ago, this Court recognized the particular need to extend comity to foreign bankruptcies. In *Canada Southern Railroad Co.* v. *Gebhard*, 109 U.S. 527 (1883), the Court held that United States bondholders of a financially embarrassed Canadian railroad were bound by a Canadian reorganization plan. 109 U.S. at 538-39. The Court observed that by dealing with a foreign corporation, the bondholders had impliedly subjected themselves to the laws of the foreign government, including its insolvency laws. *Id.* at 537. The Court further noted that absent comity, a plan of reorganization involving a corporation with multi-national creditors could never be effective:

> Unless all parties in interest, wherever they reside, can be bound by the arrangement . . . the scheme may fail. All home creditors can be bound. What is needed is to bind those who are abroad. Under these circumstances the true spirit of international comity requires that schemes of this character, legalized at home, should be recognized in other countries.

Id. at 539.

Section 304, enacted in 1978, codifies the rule of comity. It furthers the dual goals of recognizing the interest of a foreign nation in winding up the affairs of its own entities and achieving an equitable distribution of a debtor's assets, something that can only be accomplished in a single insolvency proceeding. *Cf. Victrix S.S. Co., S.A.* v. *Salen Dry Cargo A.B.*, 825 F.2d 709, 713-14 (2d Cir. 1987) ("[t]he equitable and orderly distribution of a debtor's property requires assembling all claims against the limited assets in a single

proceeding''); *Cunard Steamship Co., Ltd.* v. *Salen Reefer Services AB*, 773 F.2d 452, 458 (2d Cir. 1985) (''The granting of comity to a foreign bankruptcy proceeding enables the assets of a debtor to be disbursed in an equitable . . . manner, rather than in . . . piecemeal fashion. Consequently, American courts have consistently recognized the interest of foreign courts in liquidating or winding up the affairs of their own domestic business entities''). Indeed, the court below recognized that ''[t]he purpose of a § 304 petition is to prevent the piecemeal distribution of assets in the United States by means of legal proceedings initiated in domestic courts by local creditors'' (App. 13a). *See also* S. Rep. No. 989, 95th Cong., 2d Sess. 35, *reprinted in* 1978 U.S. Code & Admin. News 5787, 5821 (§ 304 is based on ''[p]rinciples of international comity and respect for the judgments and laws of other nations;'' its purpose is ''to prevent dismemberment by local creditors of assets located here.'')

In determining whether to grant ancillary relief, § 304(c) directs the bankruptcy court to be ''guided by what will best assure an economical and expeditious administration'' of the foreign debtor's estate. While paying lip service to the bankruptcy court's finding that the six § 304(c) factors favored granting the petition, the Second Circuit drastically curtailed the permissible scope of § 304 relief. The Second Circuit ruled that turnover can only be granted as to assets which would be property of a domestic bankruptcy ''estate'' under § 541 and that local law must be consulted to determine whether a particular asset is property of that ''estate.'' This conclusion is not consistent with the plain language of either § 304 or § 541 of the Bankruptcy Code.

Section 541, which defines an estate for purposes of a domestic bankruptcy, provides that ''[t]he commencement of a case under section 301, 302 or 303 of this title creates an estate'' and goes on to list the kinds of property of which such ''estate'' is comprised. Section 541, however, contains *no* reference to § 304 and, by its express reference to §§ 301, 302 and 303, excludes § 304 from its scope. This omission was not inadvertent; Congress plainly intended that a § 304

case not create a domestic bankruptcy "estate" requiring American administration. Consequently, § 541, by its express terms, has no application to cases commenced under § 304.

In concluding otherwise, the Second Circuit erroneously assumed that because § 304 and § 541 both contain the word "estate", each section must define the word the same way. The mere fact that two statutes share a word, however, is not enough to justify the conclusion that the words have the same meaning:

> Where the subject matter to which the words refer is not the same in the several places where they are used, or the conditions are different, or the scope of the legislative power exercised in one case is broader than that exercised in another, the meaning may well vary to meet the purposes of the law, to be arrived at by a consideration of the language in which those purposes are expressed, and of the circumstances under which the language was employed.

Atlantic Cleaners & Dyers, Inc. v. *United States*, 286 U.S. 427, 433 (1932); *see also District of Columbia* v. *Carter*, 409 U.S. 418, 421, *reh'g denied*, 410 U.S. 959 (1973). More recently, the Court recognized that even the same words used in separate paragraphs of the same provision in the Bankruptcy Code had very different meanings. *Dewsnup* v. *Timm*, ____ U.S. ____, 112 S.Ct. 773, 778, 116 L.Ed.2d 903, 911 (1992).

The Second Circuit's conclusion is also at odds with the language of § 304. In contrast to § 541 which concerns "property of *the* estate", § 304 concerns "property of *such* estate" (emphasis added). Section 304 does not refer to § 541 or to "property of *the* estate." To understand what "property of *such* estate" means it is necessary to read the phrase in context. When § 304 is read as a whole it becomes clear that "property of *such* estate" can only refer to the estate of the foreign debtor as defined by the laws of the foreign jurisdiction.

Section 304's first use of the word "estate" does not appear in the turnover arm of § 304. Rather, it occurs in the injunctive arm of the statute, § 304(b)(1)(B), which grants the bankruptcy court the power, *inter alia*, to enjoin "the commencement or continuation of any judicial proceeding to create or enforce a lien against the property of *such* estate." The dictionary definition of the word "such" requires that the phrase "such estate" refer back to a previous portion of the statute, which can only be to the phrase "such property" in § 304(b)(1)(A)(ii), the immediately preceding subparagraph. The phrase "such property" in turn refers back to the phrase "property involved in such foreign proceeding" set forth in the immediately preceding clause. *See* § 304(b)(1)(A)(i). Thus, when the phrase "property of *such estate*" next appears in § 304(b)(2), the turnover provision, it can only be a short-hand reference to the original phrase "property involved in such foreign proceeding" in § 304(b)(1)(A)(i), namely, the foreign estate as defined by the law of the foreign forum. It is undisputed that Mebco's Swiss Bank-N.Y. account is part of the property involved in the Swiss insolvency proceedings. Under the plain language of § 304, the account is within the bankruptcy court's turnover authority.

The conclusion that § 304 refers to the foreign estate—as opposed to the domestic estate created by § 541—is supported by the legislative history of § 304. The legislative history of § 304 makes no reference to § 541. Of greater significance, it shows that Congress's focus in enacting § 304 was on comity and avoiding piecemeal distributions of assets located here. Because Congress was not concerned with the administration of the foreign estate beyond the fundamental fairness considerations embodied in the six § 304(c) factors, there is no reason for Congress to have insisted that turnover be limited to that portion of a foreign estate which would have been part of the debtor's estate if the proceeding were a domestic bankruptcy case. *In re Goerg*, 844 F.2d 1562, 1567-68 (11th Cir. 1988), *cert. denied*, *Parungao* v. *Goerg*, 488 U.S. 1034 (1989) makes this point. In *Goerg*, a domestic

claimant argued against turnover on the ground that the foreign debtor, a decedent's estate, did not qualify as a "debtor" under the Code. Noting that in enacting § 304 Congress had been concerned about preventing dismemberment by local creditors of assets located in this country and *not* about actual bankruptcy administration under the Code, the Eleventh Circuit concluded that "it would make little sense to require that the subject of the foreign proceeding qualify as a 'debtor' under United States bankruptcy law." 844 F.2d at 1568.

That § 304 permits turnover of all property encompassed by the foreign estate is reinforced by the legislative history of § 306 of the Bankruptcy Code, which provides that the filing of a § 304 petition constitutes a limited appearance by the foreign representative. The legislative history of § 306 is clear that a § 304 petition concerns a foreign estate governed by foreign law:

> [This] protection [from United States jurisdiction] is necessary to allow the foreign representative to present his case and the case of the foreign estate, without waiving the normal jurisdictional rules of the foreign country. That is, creditors in this country will still have to seek redress against the foreign estate according to the host country's jurisdictional rules.

H. Rept. No. 95-595, 95th Cong., 2nd Sess. 36 (1977), *reprinted in*, 1978 U.S. Code Cong. & Admin. News 5822.

The flaw in the Second Circuit's construction of § 304 is also plain from the anomalous results it produces. If the Second Circuit's construction of § 304 is right, then the bankruptcy court can enjoin any action or the enforcement of any judgment with respect to property "involved in" a foreign proceeding under § 304(b)(1) without an antecedent adjudication of ownership rights but cannot order turnover under § 304(b)(2) without first evaluating the creditor's ownership interests under local law. There is no rational reason for Congress to have authorized bankruptcy courts to issue injunctions relating to property whether or not encompassed

by § 541 but to have forbidden turnover of property unless it falls within § 541's ambit. The Second Circuit's logic would permit a bankruptcy court to keep an action in limbo forever, permanently enjoining a creditor from prosecuting his claim, but denying the foreign representative the right to administer the funds.

Section 304 is essentially a forum selection device, premised on the principle that an equitable distribution of assets can only be achieved in a single insolvency proceeding in which the claims of *all* creditors, both domestic and foreign, can be heard under one set of rules. The proper focus of a § 304 case should be on *which* forum decides the creditor's claim not *how* that claim is adjudicated. Where there is no dispute that the debtor is the subject of a foreign insolvency proceeding, that American creditors will receive due process in the foreign tribunal, and that the disputed property is part of the property being administered abroad, the bankruptcy court's inquiry under § 304 should come to an end.

Because Congress wrote § 304 to avoid piecemeal adjudications of a foreign debtor's property, it subverts Congress's purpose in enacting § 304 to require the bankruptcy court to make a determination of the creditor's ownership claim under local property law. In permitting the interests of one domestic creditor to outweigh the interests of all others, the Second Circuit created two sets of rules—one for American creditors and one for everyone else. As one of the first cases decided under § 304 put it,

> As in [*Canada Southern Railway v. Gebhard*, 109 U.S. 527 (1883)], the liquidation laws of the Bahamas are in harmony with those of the United States and must be afforded comity. The claims by [local American creditors] that they are exempted from the Bahamian Winding-Up Rules and regulations simply because they are American creditors with possible preferences over other creditors in a New York forum must be rejected. This result is altogether just and appropriate as these creditors dealt freely with [the foreign debtor] and were

> undoubtedly aware that they were dealing with a bank incorporated under and subject to foreign law when they first began doing business with [it].

Matter of Culmer, 25 B.R. 621, 632 (Bankr. S.D.N.Y. 1982). In reaching the contrary result, the Second Circuit offended the doctrine of comity and destroyed the Code's guiding principle of equality of distribution of assets among creditors.

The final irony of the Second Circuit's approach is that it permits a creditor like Refco to fare *better* than it would in a United States bankruptcy.[2] By letting state law control

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2 In a domestic bankruptcy, a creditor like Refco would not have automatically obtained the return of his "property." For example, a creditor with a pre-petition reclamation claim must not only meet the ten-day written demand requirements of § 546(c)(1) of the Bankruptcy Code, but must also face the possibility that the debtor will be permitted to keep the goods, leaving the seller with an administrative claim against the estate, but not the return of his "property". Nor would a post-petition creditor, as Refco claims to be, necessarily obtain the return of goods delivered by it under an executory contract with the debtor. Under § 365(a) of the Bankruptcy Code, a trustee has the right to "assume or reject any executory contract . . . of the debtor." If the trustee assumes the contract, the estate keeps the property, and if the trustee rejects the contract, the seller receives only a pre-petition claim for damages. The trustee's rejection does not mean the contract is rescinded. *Cf. In re Rudaw/Empirical Software Products Ltd.*, 83 B.R. 241, 246 (Bankr. S.D.N.Y. 1988) (collecting cases).

Even establishing the elements of a constructive trust in a domestic bankruptcy does not automatically give the beneficiary complete relief. Under the majority rule, the trustee would have the right to avoid such a transfer by an exercise of the rights of the most ideal hypothetical creditor, as conferred on a bankruptcy trustee under § 544 of the Bankruptcy Code. *Cf. In re Seaway Express Corp.*, 912 F.2d 1125, 1128 (9th Cir. 1990) (collecting cases).

Indeed, in its zeal to protect an American creditor, the Second Circuit broadly construed New York law to find a constructive trust claim despite the absence of any fiduciary duty of the debtor to Refco, an element generally required to impose a constructive trust. The court's expansive treatment of the constructive trust remedy suggests that there will be a substantial number of creditors who will be able to insist on a threshold adjudication of ownership under the Second Circuit's rule.

Refco's claim, the Second Circuit not only demeaned the Swiss sovereign's right to liquidate the affairs of its own debtor, it permitted an unsecured creditor to escape the community aspects of bankruptcy law altogether. This kind of loophole is not likely to be lost on creditors in transnational bankruptcies. The Second Circuit's ruling offers domestic creditors a substantial incentive to do exactly what Refco did—obtain *ex parte* attachments against the foreign debtor's assets in the hope of obtaining an advantage over other creditors. This is exactly what § 304 was intended to forbid.[3]

2. If A Threshold Determination of Property Rights Is Proper, It Should Be Governed By Swiss Law

Under the superior interests test applied to choice of law questions in cases such as this, *see Wells Fargo Asia Ltd.* v. *Citibank, N.A.*, 936 F.2d 723, 726 (2d Cir. 1991), *cert. denied*, 60 U.S.L.W. 3360 (U.S. June 22, 1992) (No. 91-689), there is no question that Switzerland has an interest superior to the United States in having Swiss law applied to the liquidation of a Swiss bank. Switzerland "has by far the greatest interest in [the Swiss debtor's] liquidation since neither the United States nor the State of New York has any governmental or public interest in [the Swiss debtor's] liquidation." *Matter of Culmer*, 25 B.R. at 628-29. Indeed, the Second Circuit acknowledged that the "Swiss liquidator is concerned with marshalling Mebco's assets and looking after the interests of Mebco's many creditors. Undeniably Swiss concerns

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3 The Second Circuit's rule will also have the effect of substantially delaying the administration of transnational bankruptcy proceedings. If ownership of assets located here must be adjudicated prior to turnover, distribution in the primary foreign liquidation case will be delayed until the discovery, trial and appeal of the threshold issue of ownership are completed. The result would be to burden bankruptcy courts here with complicated discovery disputes in a transnational setting, while imposing delay and uncertainty on the main body of creditors entitled to distribution in the foreign proceeding. Section 304 (c)'s purpose to "assure an economical and expeditious administration" of the foreign debtor's estate would obviously be thwarted by such a result.

will be affected by the outcome of the current dispute" (App. 20a).

Mebco's contacts with New York were bare indeed. Mebco officials did not come there; meetings with Refco did not take place there; Mebco did not maintain an office there; Mebco was not licensed to do business there. Every time Refco wanted to meet with Mebco, it went to Geneva. All Mebco did in New York was to pass local currency through a correspondent bank account. And for each transfer in this country, there was a corresponding transfer in Europe. If a determination concerning property interests must be made, Swiss law is the applicable law.

3. The Questions Presented By this Petition Are Ripe for Review

The questions presented to the Court are appropriate for review now even though they come to the Court on interlocutory appeal. This Court has granted certiorari, where, as here, the judgment below is not final, but the questions presented are important and "fundamental to the further conduct of the case". *See e.g.*, *United States* v. *General Motors Corp.*, 323 U.S. 373, 377 (1945). The questions presented here are obviously "fundamental to the further conduct of the case" since a reversal will obviate the "threshold determination" of Refco's state-law claims, the sole purpose of the remand. Moreover, if the Court does not grant the petition, it may never get the opportunity to consider the issue whether a "threshold determination" is necessary. If the Second Circuit's decision goes unreviewed, regardless of which party prevails on remand, the issue of whether a "threshold determination" of property rights is required under § 304 may well become moot. Finally, the questions are ripe for adjudication by this Court now because the proceedings on remand will only concern Refco's state-law rights and will not affect the issues presented here.

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

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July 7, 1992

APPENDIX

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 651—August Term, 1991

(Argued: November 21, 1991 Decided: April 9, 1992)

Docket No. 91-5061

IN RE: KOREAG, CONTROLE et REVISION S.A., as Official Liquidator of Mebco Bank, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

KOREAG, CONTROLE et REVISION S.A.,

Petitioner-Appellee,

—against—

REFCO F/X ASSOCIATES, INC.,

Respondent-Appellant.

Before:

PRATT, MAHONEY, and MCLAUGHLIN,

Circuit Judges.

Appeal from a revised order of the United States District Court for the Southern District of New York, Whitman Knapp, *Judge*, entered September 16, 1991 that affirmed an order of the United States Bankruptcy Court for the Southern District of New York. The bankruptcy court order granted summary judgment directing the turnover of certain assets to petitioner-appellee, liquidator in a Switzerland insolvency proceeding, and enjoining the continuation by respondent-appellant of a related lawsuit pursuant to 11 U.S.C. § 304 (1988).

We vacate and remand.

JACK WEINBERG, New York, New York (Marianne Bretton-Granatoor, Therese M. Doherty, Graubard Mollen Horowitz Pomeranz & Shapiro, New York, New York, of counsel), *for Respondent-Appellant*.

CELIA GOLDWAG BARENHOLTZ, New York, New York (Richard A. Edlin, Kronish, Lieb, Weiner & Hellman, New York, New York, of counsel), *for Petitioner-Appellee*.

MAHONEY, *Circuit Judge*:

Respondent-appellant Refco F/X Associates, Inc. ("Refco") appeals from an order of the United States District Court for the Southern District of New York, Whitman Knapp, *Judge*, entered September 16, 1991. That order affirmed an order of the United States Bankruptcy

Court for the Southern District of New York, Cornelius Blackshear, *Bankruptcy Judge*, that granted summary judgment in favor of petitioner-appellee Koreag, Controle et Revision S.A. ("Koreag"), liquidator in a Swiss insolvency proceeding, on Koreag's petition pursuant to 11 U.S.C. § 304 (1988); ordered the turnover to Koreag of certain funds deposited in a New York bank account; and enjoined the continuation of a related lawsuit by Refco.

We vacate and remand, concluding that the district court and bankruptcy court should have made a threshold determination whether certain disputed funds in the bank account were "property of [the insolvent] estate" within the meaning of 11 U.S.C. § 304(b)(2) (1988).

Background

This action arises from a series of currency exchange transactions that took place in April 1989. The issue on this appeal concerns the parties' respective interests in funds deposited in a New York bank account in connection with these exchanges.

A. *The Transactions at Issue.*

Much that follows has been stipulated by the parties. Refco is a corporation that engages in commodity and currency transactions around the world. It is organized under the laws of New York, and has its principal place of business in New York City. Mebco Bank, S.A. ("Mebco") is a Swiss bank currently in bankruptcy liquidation under the laws of Switzerland. Prior to liquidation, Mebco engaged in worldwide banking activities, including the trading of currencies.

Koreag is a Swiss corporation which has been appointed liquidator in charge of administering the distribution of Mebco's estate. Under Swiss law, Koreag is the sole entity authorized to act on behalf of Mebco. Swiss Bank Corporation is a Swiss bank whose New York branch office ("Swiss Bank-N.Y.") is the locus of the bank account in which are deposited the funds at issue in this action.

Refco and Mebco first discussed doing business together at a meeting in Geneva, Switzerland in May 1986 between a Mebco representative and a representative of Refco's London office. Mebco subsequently provided its annual reports for 1986 and 1987 to Refco. On June 3, 1988, Refco granted Mebco a ten million dollar line of credit to be used for daily settlement of currency transactions.

Refco and Mebco engaged in extensive currency transactions beginning in June 1988. The trading of currencies was accomplished by direct communication between two dealers to determine the terms of the exchange: the currencies involved, the amounts, the exchange rate, and the banks to be used. The exchange was then consummated several days later by wire transfers of currencies in accordance with the prior agreement.

The currency exchanges conducted by Refco and Mebco were of two varieties, in both of which (according to the stipulation of the parties) "Refco and Mebco were each, at once, a purchaser and seller of currencies." The parties have also stipulated that "[t]he agreements between Refco and Mebco contemplated simultaneous exchanges of currencies."

One type of transaction involved Refco's selling foreign currency to Mebco in exchange for U.S. dollars. In

that event, Refco would wire transfer the foreign currency into Mebco's account at a designated European bank. Mebco in turn would wire U.S. dollars into an account that Mebco maintained at Swiss Bank-NY (the "Account") with instructions to credit a Refco account at Citibank in New York. Alternatively, Refco purchased foreign currency from Mebco. In that case, the transaction would proceed in reverse, with Refco wiring U.S. dollars to the Account, and Mebco transferring foreign currency to a designated Refco bank account in Europe.

Refco and Mebco entered into several currency exchange contracts during the period April 20 to April 27, 1989. In partial settlement thereof, Refco wired $7,407,510 to the Account at 3:52 p.m. Eastern Standard Time[1] on April 28, 1989, in exchange for which Refco was to receive from Mebco foreign currencies of comparable value, to be delivered to Refco bank accounts abroad. Refco also delivered foreign currencies worth approximately 4.1 million dollars to Mebco European accounts from April 28 to May 2, 1989, and in exchange was to receive that amount in U.S. dollars from Mebco via the Account. In connection therewith, from April 20 to April 27, 1989, Mebco had transmitted orders to Swiss Bank-NY for payments from the Account to Refco's account at Citibank in the total amount of $8,789,800. Each of the individual trades was subject to approval by Refco's New York office, which sent confirmation slips for each transaction to Mebco in Switzerland.

At 10:15 A.M. on April 27, 1989, however, the Swiss Banking Commission of Switzerland placed Mebco into liquidation under Swiss law. Immediately thereafter, Koreag was appointed as liquidator. At approximately

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1 All times herein are Eastern Standard Time.

2:00 p.m. that day, in accordance with instructions from its Geneva office, Swiss Bank-N.Y. stopped all payments out of the Account, including the payments intended as performance for the Refco currency exchanges. Swiss Bank-NY received no instruction to stop receiving incoming transfers, on the other hand, and the Account remained open to receive deposits.

Refco was not informed by Debtor, Koreag, or Swiss Bank-NY that Debtor had been placed in liquidation, that the Account was closed to outgoing payments, or that Mebco would not perform its side of most of the pending currency exchanges.[2] The commencement of the liquidation proceedings was reported by the Dow Jones International News Service newswire, but Refco does not subscribe to that service, and claims that it never received notice that Mebco was in liquidation and its payment orders had been stopped.

Refco received a portion of the foreign currencies covered by its April 28 transfer to the Account of $7,407,510, but the remaining foreign currencies—corresponding to approximately 6.9 million of the U.S. dollars delivered to Mebco—were never delivered. Similarly, there has been no delivery to Refco of U.S. dollars in exchange for the foreign currencies worth approximately 4.1 million dollars that Refco delivered to Mebco European accounts from April 28 to May 2, 1989, although funds had been provided to the Account by Mebco for that purpose. The net result of these aborted currency exchanges is that

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2 As will appear, Refco received a small portion of the foreign currencies covered by its April 28 transfer to the Account of $7,407,510. In addition, the parties have stipulated that at 3:46 p.m. on April 27, 1989, after Mebco was placed into liquidation, Refco wired two million dollars to the Account for which it received the agreed foreign currencies in exchange.

Refco transferred approximately 6.9 million dollars into the Account, and approximately 4.1 million dollars worth of foreign currency to overseas Mebco accounts, for which Mebco failed to make reciprocating transfers.[3]

On May 3, 1989, Refco first learned of Mebco's financial situation in response to an inquiry into Mebco's failure to perform its side of the pending currency exchanges. During this conversation between Gary M. Weiss, senior vice president of Refco, and a Mr. Savio to whom Weiss was referred when he called Mebco in Geneva, Weiss orally demanded that Mebco return the U.S. dollars and foreign currencies that Refco had delivered to Mebco in connection with those exchanges. Thereafter, also on May 3, Citibank sent a telex message on behalf of Refco to Swiss Bank-NY requesting the return, *inter alia*, of the disputed 6.9 million dollars previously wired to the Account by Refco on April 28, 1989. Swiss Bank-NY responded by telex on May 4, 1989 that it would release the funds when authorized by Koreag to do so. Koreag never provided authorization, however, and the funds were never released.

Also on May 4, 1989, Weiss wrote a letter to Mebco, c/o Koreag, detailing "the amounts that are claimed from [Mebco] by [Refco] as of May 4, 1989." Further, *see infra*, a litigation affidavit by Weiss dated May 4, 1989 and served upon Mebco reiterated Refco's claim.

B. *The Proceedings Below.*

On May 5, 1989, Refco commenced an action against Mebco in the United States District Court for the Southern District of New York to recover the Disputed Funds.

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3 The precise amount in dispute is $11,191,334.52 (the "Disputed Funds").

At the same time, Refco obtained an *ex parte* attachment of the Account. In support of the attachment, Refco served Koreag with papers that included an affidavit by Weiss dated May 4, 1989 which repeated Refco's claim and demand against Mebco, and attached as an exhibit Weiss' letter to Mebco, c/o Koreag, dated May 4, 1989. The attachment papers were delivered to an air courier for transmission to Mebco, and also mailed to Mebco, on May 5, 1989, and the courier completed its delivery to Mebco on May 8, 1989.

Refco moved the district court to confirm the attachment, and Koreag, intervening as Mebco's successor-in-interest, cross-moved to dismiss Refco's action. Koreag's position was that comity should be accorded to the Swiss insolvency proceeding, and that all the funds in the Account should accordingly be turned over for administration in Switzerland. The district court concluded that a proceeding pursuant to 11 U.S.C. § 304 (1988)[4] was the

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4 Section 304 provides:

(a) A case ancillary to a foreign proceeding is commenced by the filing with the bankruptcy court of a petition under this section by a foreign representative.

(b) Subject to the provisions of subsection (c) of this section, if a party in interest does not timely controvert the petition, or after trial, the court may—

(1) enjoin the commencement or continuation of—

(A) any action against—

(i) a debtor with respect to property involved in such foreign proceeding; or

(ii) such property; or

(B) the enforcement of any judgment against the debtor with respect to such property, or any act or the commencement or continuation of any judicial proceeding to create or enforce a lien against the property or such estate;

appropriate vehicle for determining whether to defer to the Swiss insolvency proceedings, and invited Koreag to initiate such a proceeding by application to the bankruptcy court.

Koreag promptly petitioned the bankruptcy court for relief ancillary to a foreign proceeding pursuant to § 304. The petition alleged that the "economical, expeditious and equitable administration of Mebco's liquidation governed by the insolvency laws of Switzerland" required that Mebco's assets in the United States be marshalled and turned over to Swiss insolvency authorities to "prevent the dismemberment of Mebco's estate, to avoid preferences, and to ensure the equitable administration of [the] estate[.]" The petition sought an injunction against further

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(2) order turnover of the property of such estate, or the proceeds of such property, to such foreign representative; or

(3) order other appropriate relief.

(c) In determining whether to grant relief under subsection (b) of this section, the court shall be guided by what will best assure an economical and expeditious administration of such estate, consistent with—

(1) just treatment of all holders of claims against or interests in such estate;

(2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;

(3) prevention of preferential or fraudulent dispositions of property of such estate;

(4) distribution of proceeds of such estate substantially in accordance with the order prescribed by this title;

(5) comity; and

(6) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

attempts by Refco to reach the funds in the Account, and an order turning over the Account to Koreag as liquidator pursuant to § 304(b)(2).

By decision entered August 26, 1991, the bankruptcy court granted summary judgment to Koreag. *In re Koreag, Controle et Revision S.A.*, 130 B.R. 705 (Bankr. S.D.N.Y. 1991). In reaching its decision, the court first rejected Refco's contention that the court lacked jurisdiction over the property sought by Koreag, i.e., the funds on deposit at the Account. *Id.* at 710-12.

Refco argued that before property could be turned over pursuant to § 304(b)(2), the court must determine that the property was part of the debtor's estate; in other words, the debtor's property. The bankruptcy court declined to make a threshold finding as to who owned the property, stating that Refco's argument "plac[ed] the proverbial 'cart before the horse.' " *Id.* at 711. The court initially stated that in order to establish jurisdiction to proceed pursuant to § 304, it need only be established that: "(1) a foreign proceeding was commenced against the debtor; (2) the petitioner is a foreign representative entitled to file the action under section 304; and (3) 'the debtor had certain assets within the judicial district where the petition was filed.' " *Id.* at 711 (quoting *In re Trakman*, 33 B.R. 780, 783 (Bankr. S.D.N.Y. 1985)).

The court then declined to decide the need to satisfy the third (quoted) requirement, however, *see* 130 B.R. at 711 n.3 (citing *In re Metzeler (Metzeler v. Bouchard Transp. Co.)*, 78 B.R. 674 (Bankr. S.D.N.Y. 1987)), because it deemed that requirement, in any event, fulfilled in this case. The court ruled that "when conducting a jurisdictional analysis, the laws in the foreign proceeding are determinative of whether the foreign bankrupt has assets

located in the district in which the section 304 petition was filed," 130 B.R. at 711, and "[u]nder Swiss law, the funds in [the Account] are included in the property involved in Mebco's liquidation proceedings." 130 B.R. at 712. The court concluded: "The last jurisdictional requirement is satisfied since the funds are located in this district." *Id.*[5]

The bankruptcy court next evaluated the turnover request in light of the policy considerations set forth in § 304(c). The court stated that "[c]omity is inevitably the more significant factor since the other factors (except for the sixth element dealing with the fresh start theory) are inherently taken into account when considering comity." 130 B.R. at 712 (citing *In re Culmer*, 25 B.R. 621, 629 (Bankr. S.D.N.Y. 1982)). Concluding that the laws of Switzerland were "not repugnant and violative of our fundamental notions of fairness," *id.* at 716, and that the "marshalling of Mebco's assets should be conducted in one forum with one set of laws so as to ensure equality among all of the creditors," *id.*, the bankruptcy court granted summary judgment directing that the funds in the Account be turned over to Koreag. *Id.* Although the bankruptcy court's opinion stated that "the balance of [Koreag's] requests in its motion are denied in light of this Court's decision to turnover the funds," *id.*, the order entered by the bankruptcy court permanently enjoined Refco from pursuing the action it had initiated against

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5 There were concededly funds in the Account, when Koreag initiated the § 304 proceeding, in addition to those claimed by Refco, so we can see no impediment to the bankruptcy court's exercise of jurisdiction over that proceeding under any view of the jurisdictional issue. As will appear, however, we disagree with the bankruptcy court's conclusion that the threshold determination of the ownership of the funds in the Account claimed by Refco is to be made under Swiss law.

Mebco in the district court, in addition to directing turnover of the Account to Koreag.

The district court then entered an order on September 13, 1991, revised on September 16, 1991, that affirmed the bankruptcy court order "on Judge Blackshear's opinion below," but stayed enforcement of the order of the district court "until September 30, 1991 at 5:00 p.m. to permit [Refco] to apply to the Court of Appeals for a further stay." Refco thereupon appealed, and on October 1, 1991, this court granted a further stay directing "that the principal amount of $11,191,334.52 [*see supra* note 3], together with interest on that amount from May 5, 1989, . . . be held by Swiss Bank pending final determination of Refco's appeal . . . , and may not be transferred to Koreag," and expedited the appeal.

Discussion

We begin by noting that we will review the decision of the bankruptcy court (and of the district court affirming on the opinion of the bankruptcy court) *de novo* because the questions presented are matters of statutory interpretation. *See Truck Drivers Local 807 v. Carey Transp. Inc.*, 816 F.2d 82, 88 (2d Cir. 1987).

Refco presents two arguments on appeal. First, Refco contends that because Refco had a superior property interest in the Disputed Funds, they were not "property of [Mebco's] estate" within the meaning of § 304(b)(2), and the bankruptcy and district courts accordingly erred in ordering their turnover to Koreag. Refco's alternative position is that even if the Disputed Funds were part of Mebco's estate, the bankruptcy and district courts incorrectly applied the factors set forth in § 304(c) in fashioning the turnover remedy.

We first turn to Refco's argument based upon § 304(b)(2). Responding to Refco's contentions, we initially consider whether, when an adverse claimant raises a plausible dispute concerning the ownership of property whose turnover is sought by a foreign liquidator pursuant to § 304(b)(2), a court should resolve that threshold issue before ordering turnover. Answering that question in the affirmative, we next consider what law governs the resolution of the ownership issue. Concluding that New York law provides the rule of decision in this case, we then address the § 304(b)(2) issue in terms of (1) the New York law of constructive trusts, and (2) the New York Uniform Commercial Code.

A. *Threshold Determination of Ownership Issue.*

Section 304(a) authorizes a "foreign representative" in a "foreign [bankruptcy] proceeding" to commence a "[c]ase ancillary to [that] proceeding" in a United States bankruptcy court to protect the administration of the foreign proceeding. The purpose of a § 304 petition is to prevent the piecemeal distribution of assets in the United States by means of legal proceedings initiated in domestic courts by local creditors. *Victrix S.S. Co., S.A. v. Salen Dry Cargo A.B.*, 825 F.2d 709, 713-14 (2d Cir. 1987); *Cunard S.S. Co. v. Salen Reefer Servs. AB*, 773 F.2d 452, 454-55 (2d Cir. 1985). A bankruptcy court is given broad latitude in fashioning an appropriate remedy in a § 304 proceeding. *In re Axona Int'l Credit & Commerce Ltd.*, 88 B.R. 597, 606 (Bankr. S.D.N.Y. 1988), *aff'd*, 115 B.R. 442 (S.D.N.Y. 1990), *appeal dismissed*, 924 F.2d 31 (2d Cir. 1991); *In re Culmer*, 25 B.R. at 624; *see also* S. Rep. No. 989, 95th Cong., 2d Sess. 35 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5821 (§ 304(c) "guidelines are designed to give the court the maximum flexibility in handling ancillary cases").

We nonetheless disagree with the bankruptcy court's ruling in this case that a turnover was properly ordered upon the *de minimis* showing that the disputed funds in the Account were "included in the property involved in Mebco's liquidation proceedings, . . . [and] located in this district." 130 B.R. at 712. The court rejected the notion that it was required to make a threshold finding as to the ownership of the funds prior to issuance of the turnover order. In our view, this was not a proper reading of § 304(b)(2).

The applicable distinction is drawn in Lawrence P. King, 2 *Collier on Bankruptcy* ¶ 304.01, at 304-3 (15th ed. 1992) (emphasis added): "For purposes of section 304, the estate of a foreign debtor is defined by the law of the jurisdiction in which the foreign proceeding is pending, *with other applicable law serving to define the estate's interest in particular property.*" *See also In re Lines*, 81 B.R. 267, 271 (Bankr. S.D.N.Y. 1988) (same).

This interpretation of § 304(b)(2) is supported by the language of the statute. While § 304(b)(1) empowers a bankruptcy court to enjoin litigation "with respect to property involved in" a foreign insolvency proceeding, presumably "to prevent dismemberment by local creditors of assets located here," S. Rep. No. 989 at 35, § 304(b)(2) authorizes turnover only of "property of such estate, or proceeds of such property." Thus, the use of the term "property of such estate" presupposes an antecedent determination of property interests as a condition to the turnover of property to a foreign representative.

This analysis finds further support in the analogy provided by the related provisions of federal bankruptcy law applicable to domestic cases. In a domestic bankruptcy, the commencement of a case creates a bankruptcy estate.

11 U.S.C. § 541(a) (1988). The estate is defined to comprise "all legal or equitable interests of the debtor in property as of the commencement of the case" (with exceptions not pertinent here), which definition is supplemented by a listing of several more specifically described categories of property interests. *Id.* § 541 (a)(1)-(7). Nonetheless, "[a] lthough federal bankruptcy law determines the outer boundary of what may constitute property of the estate, state law determines the 'nature of a debtor's interest' in a given item." *In re Crysen/Montenay Energy Co. (Crysen/Montenay Energy Co. v. Esselen Assocs., Inc.)*, 902 F.2d 1098, 1101 (2d Cir. 1990) (quoting *In re Howard's Appliance Corp. (Sanyo Elec., Inc. v. Howard's Appliance Corp.)*, 874 F.2d 88, 93 (2d Cir. 1989)).

We see no reason why a similar allocation as to controlling law should not apply in § 304 cases. Property interests have an independent legal source, antecedent to the distributive rules of bankruptcy administration, that determines in the first instance the interests of claimant parties in particular property. It logically follows that before a particular property may be turned over pursuant to § 304(b)(2), a bankruptcy court should apply local law to determine whether the debtor has a valid ownership interest in that property when the issue is properly posed by an adverse claimant.

Koreag advances two objections to such application of local law by a bankruptcy court. Its first argument, that § 304 permits the turnover of any property "involved in" a foreign bankruptcy, is simply at odds with the relevant statutory language. Although Congress provided in § 304(b)(1) for certain injunctions to be issued regarding property "involved in" a foreign insolvency proceeding, § 304(b)(2) authorizes turnover only of "property of [the]

estate" in a foreign proceeding. Thus, Congress used different language in § 304(b)(1) and (2), the two provisions perform different functions, and we are not at liberty to ignore this legislative choice.

Koreag next contends that if local law is to be applied, the foreign forum presiding over the insolvency estate, and not a local bankruptcy court, should apply that law. Koreag presses the point that adjudication of creditors' claims in a U.S. court will deprive other creditors of an opportunity to be heard, and defeat the policy of distribution by a single forum which § 304 is designed to ensure. In this connection, Koreag cites *In re Lines*, 81 B.R. at 272, for the proposition that Refco's claims should be adjudicated in the Swiss proceeding. We find these arguments unavailing.

Koreag, as liquidator, has asked a United States bankruptcy court to require the turnover of disputed assets to a foreign insolvency proceeding. The power of the court extends to "property of [the] estate." § 304(b)(2). Once a plausible challenge is presented as to whether particular property falls within the statutory definition, the bankruptcy court whose authority is invoked must determine the legitimacy of that invocation. The nature of this determination demands that it be made prior to the turnover of the property. It is unsatisfactory to say that the property should first be turned over, because it is the ascertainment that property is "of [the] estate" under local law that defines the extent of the court's power to issue the turnover order.

It is also not the case that Mebco's other creditors are prejudiced by such a threshold determination as to property ownership. Refco is not merely asserting rights as an ordinary creditor or claimant in a bankruptcy proceeding.

Its position is that Mebco does not own the Disputed Funds. A determination that the funds are not property of the estate therefore does not improperly affect other creditors of the estate, because they have valid claims only against the estate's bona fide assets. The situation is clearly distinguishable from an effort by a normal bankruptcy creditor, without any plausible ownership claim to a specific asset, to gain a preferred position vis-a-vis other creditors by initiating a separate legal proceeding. *Cf. Victrix*, 825 F.2d at 714 (refusal to countenance attachment designed to evade writ of Swedish bankruptcy court); *Cunard*, 773 F.2d at 456 (same).

Finally, *In re Lines* does not support Koreag's position. That case involved an injunction under § 304 (b)(1), utilizing the broader "involved in" standard of that provision. *See* 81 B.R. at 272. Nevertheless, the court *did* engage in a threshold determination of local law, holding that the particular property at issue, an insurance fund, was sufficiently connected to the debtor under New York law to be "involved in" the foreign insolvency proceeding. *See id.* at 271. We similarly conclude that particular property must be determined to be "of [the] estate" before it may be turned over pursuant to § 304(b)(2).

B. *Choice of Law.*

Having held that local law determines whether particular property is part of a debtor's estate, we must decide what local law will supply the substantive rule. Refco argues that New York is the jurisdiction whose law is controlling, while Koreag counters that Switzerland should provide the rule of decision.

Preliminarily, we are faced with an apparent problem of what choice-of-law rule to apply. Federal courts sitting in diversity jurisdiction are required by *Klaxon Co. v. Sentor Electric Manufacturing Co.*, 313 U.S. 487, 496 (1941), to apply the choice-of-law doctrines of the forum state. Many bankruptcy courts have read *Klaxon* as imposing the forum state's choice-of-law rules on bankruptcy adjudications where the underlying rights and obligations are defined by state law. *See, e.g., In re Chanel Fin., Inc. (Continental Cas. Co. v. Kellogg)*, 102 B.R. 549, 550 (Bankr. N.D. Tex. 1988); *In re O.P.M. Leasing Servs., Inc. (Hassett v. Far West Fed. Sav. & Loan Ass'n)*, 40 B.R. 380, 391-92 (Bankr. S.D.N.Y.), *aff'd*, 44 B.R. 1023 (S.D.N.Y. 1984); *In re Shepard (Central Trust Co. v. Shepard)*, 29 B.R. 928, 931 (Bankr. M.D. Fla. 1983). In contrast, federal principles should guide our consideration of which jurisdiction's substantive law applies in cases arising out of federal law. *See Corporacion Venezolana de Fomento v. Vintero Sales Corp.*, 629 F.2d 786, 795 (2d Cir. 1980), *cert. denied*, 449 U.S. 1080 (1981). This is especially appropriate when a case involves controversies implicating important federal bankruptcy policy. *Cf. Fore Improvement Corp. v. Selig*, 278 F.2d 143, 147 (2d Cir. 1960) (Friendly, J., concurring) (absent "overriding bankruptcy policy," state law applies to state-created claims under former Bankruptcy Act).

Selecting the appropriate conflicts rules would thus seem to require us to characterize the present issue under § 304(b)(2) as either predominantly founded upon state-created rights, or involving important concerns implicating national bankruptcy policy. For purposes of this appeal, however, we need not untangle the interwoven features of state and federal law, for we discern no sig-

nificant difference between the applicable federal and New York choice-of-law rules.

The federal common law choice-of-law rule is to apply the law of the jurisdiction having the greatest interest in the litigation. *See Wells Fargo Asia Ltd. v. Citibank, N.A.*, 936 F.2d 723, 726-27 (2d Cir. 1991), *petition for cert. filed*, 60 U.S.L.W. 3360 (U.S. Oct. 24, 1991) (No. 91-689); *Corporacion Venezolana de Fomento*, 629 F.2d at 795. The goal of this analysis is to evaluate the various contacts each jurisdiction has with the controversy, and determine which jurisdiction's laws and policies are implicated to the greatest extent.

New York law provides " 'that "the law of the jurisdiction having the greatest interest in the litigation will be applied and that the facts or contacts which obtain significance in defining State interests are those which relate to the purpose of the particular law in conflict." ' " *Wells Fargo Asia Ltd.*, 936 F.2d at 726 (quoting *Wells Fargo Asia Ltd. v. Citibank, N.A.*, 695 F. Supp. 1450, 1453 (S.D.N.Y. 1988) (quoting *Intercontinental Planning, Ltd. v. Daystrom, Inc.*, 24 N.Y.2d 372, 382, 248 N.E.2d 576, 582, 300 N.Y.S.2d 817, 825 (1969))). The federal and New York doctrines " 'invoke[ ] similar considerations.' " *Wells Fargo Asia Ltd.*, 936 F.2d at 726 (quoting *Wells Fargo Asia Ltd.*, 695 F. Supp. at 1453 (citing *Corporacion Venezolana de Fomento*, 629 F.2d at 725)).

Accordingly, we apply an interest analysis consistent with the law of either jurisdiction. Both New York and Switzerland have an interest in the litigation before this court. On the one hand, Refco is incorporated under the laws of New York, with its principal place of business in New York City. Refco performed its obligations under the contract, including confirming the individual transactions,

from its New York offices. The Disputed Funds and the Account are located in New York. Moreover, New York as a world financial center has a special concern with transactions such as occurred here and spawned this litigation. *See Wells Fargo Asia Ltd.*, 936 F.2d at 726-27. On the other hand, Switzerland has a valid interest in the administration of Mebco's bankruptcy estate. The Swiss liquidator is concerned with marshalling Mebco's assets and looking after the interests of Mebco's many creditors. Undeniably, Swiss concerns will be affected by the outcome of the current dispute.

Despite connections to both jurisdictions, we conclude that New York has a superior interest in the particular question at issue here. New York's concerns relate to the underlying property claims at stake, the corresponding contract rights of the parties, and the conduct giving rise to this particular property dispute. These relationships are ordinarily regulated under New York law, and New York is concerned with how this law operates as to a New York corporation with its principal place of business in New York. Switzerland's interests, on the other hand, focus less upon the ownership of particular property than upon the fair and organized administration of the debtor's estate, once defined.

The legal policy of fair and efficient distribution of a debtor's estate is distinct from the policy of how various property rights are determined. In the same way that the question is bifurcated under United States bankruptcy law —with state law defining property interests and federal law providing the scheme of distribution—the interests of the competing jurisdictions should be bifurcated in choice-of-law analysis. Switzerland's primary interest is in the administration of Mebco's insolvency estate. New York's primary interest is in defining and protecting the

property interests of its citizens and those who do business there. Thus, New York law is more closely related to the particular property dispute at issue. We conclude that New York law should apply.[6]

C. *New York Law.*

Our rulings that (1) a threshold determination as to ownership of the Disputed Funds should have been made, (2) applying New York law, require us to vacate the affirming order of the district court. We now apply New York law to address Refco's claims that it has a superior ownership interest in the particular property subject to this litigation. To the extent that these claims depend upon the resolution of legal issues, we will consider those issues at this juncture to facilitate their definitive resolution upon remand. *See United States v. Borello*, 766 F.2d 46, 60 n.23 (2d Cir. 1985). Conversely, insofar as determinations of fact must be made in order to adjudicate the claims of the parties, we shall remand to the district court for proceedings not inconsistent with this opinion.

As indicated earlier, Refco has advanced contentions premised upon (1) the New York law of constructive trusts, and (2) the New York Uniform Commercial Code. We turn initially to the constructive trust issue, for that question is at least potentially dispositive as to the ownership of all the Disputed Funds.

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6 Refco argues on appeal that the bankruptcy court lacked an adequate basis for its conclusion that "[u]nder Swiss law, the [Disputed Funds] are included in the property involved in Mebco's liquidation proceedings." 130 B.R. at 712. Our conclusion that Swiss law does not govern this controversy moots the contention.

1. *Constructive Trust.*

Refco argues that the Disputed Funds are not property of Mebco's estate because Mebco obtained them by fraud, and the funds should therefore be impressed with a constructive trust in Refco's favor. Specifically, Refco contends that fraud was committed (1) by Mebco's concealment of its deteriorating financial condition following previous representations of financial health which induced Refco to transfer currency to the Account and to Mebco's overseas bank accounts; and (2) by Mebco and Koreag, as liquidator, in that they took Refco's money post-liquidation knowing that Mebco was insolvent and incapable of performing its end of the bargained-for exchange, and without notifying Refco of the liquidation. Refco further alleges that such conduct contravenes equity and good conscience, and results in substantial unjust enrichment of Mebco's insolvency estate. Refco maintains that a constructive trust is "necessary to satisfy the demands of justice." *Latham v. Father Divine*, 299 N.Y. 22, 27, 85 N.E.2d 168, 170 (1949).

As we noted in *In re Howard's Appliance Corp.*:

> [T]he Supreme Court has declared that, while the outer boundaries of the bankruptcy estate may be uncertain, "Congress plainly excluded property of others held by the debtor in trust at the time of the filing of the petition," [*United States v.*] *Whitting Pools*, [*Inc.*, 462 U.S. 198, 205 n.10, 103 S. Ct. 2309, 2314 n.10 (1983)]; *see* S.Rep. No. 989, 95th Cong., 2d Sess. 82 *and* H.R.Rep. No. 595, 95th Cong., 2d Sess. 368, *reprinted in* 1978 U.S.Code Cong. & Ad. News 5787, 5868, 6323-24; *see also In re Kennedy & Cohen, Inc.*, 612 F.2d 963, 965 (5th Cir.) (under previous bankruptcy statute, property held by debtor in

> constructive trust "belongs to the beneficiary and never becomes a part of the bankruptcy estate"), *cert. denied*, 449 U.S. 833, 101 S.Ct. 103, 66 L.Ed.2d 38 (1980). A constructive trust, therefore, "confers on the true owner of the property an equitable interest in the property superior to the trustee's," [*In re*] *Quality Holstein Leasing*, 752 F.2d [1009, 1012 (5th Cir. 1985)]; *cf. In re General Coffee Corp.*, 828 F.2d 699, 706 (11th Cir. 1987) (constructive trust beneficiary has priority to trust assets over a judicial lienholder or execution creditor), *cert. denied*, [485] U.S. [1007], 108 S.Ct. 1470, 99 L.Ed.2d 699 (1988).

874 F.2d at 93 (footnote omitted).

The foregoing authorities deal with domestic bankruptcies, where the bankruptcy estate is defined to include, *inter alia*, "all legal or equitable interests of the debtor in property as of the commencement of the case," 11 U.S.C. § 541(a)(1), but to exclude "any power that the debtor may exercise solely for the benefit of an entity other than the debtor." *Id.* § 541(b)(1). We believe, however, that they should also govern determinations regarding "the property of [a bankruptcy] estate" under § 304(b)(2), and accordingly that Refco should be given the opportunity to present its constructive trust theory in a trial setting. The courts below never reached this issue, so we hear this appeal without an adequate factual record for its resolution. Accordingly, after setting forth the applicable principles of New York law, we will leave the definitive resolution of this issue for determination upon remand.

Under New York law, a party claiming entitlement to a constructive trust must ordinarily establish four elements: (1) a confidential or fiduciary relationship; (2) a promise, express or implied; (3) a transfer made in reliance on that

promise; and (4) unjust enrichment. *See Bankers Sec. Life Ins. Soc'y v. Shakerdge*, 49 N.Y.2d 939, 940, 406 N.E.2d 440, 440, 428 N.Y.S.2d 623, 624 (1980); *Simonds v. Simonds*, 45 N.Y.2d 233, 241-42, 380 N.E.2d 189, 194, 408 N.Y.S.2d 359, 363 (1978); *Sharp v. Kosmalski*, 40 N.Y.2d 119, 121, 351 N.E.2d 721, 723, 386 N.Y.S.2d 72, 75 (1976). Although these factors provide important guideposts, the constructive trust doctrine is equitable in nature and should not be "rigidly limited." *Simonds*, 45 N.Y.2d at 241, 380 N.E.2d at 194, 408 N.Y.S.2d at 363; *see also Bankers Sec. Life Ins. Soc'y*, 49 N.Y.2d at 940, 406 N.E.2d at 440, 428 N.Y.S.2d at 624 (application of doctrine to particular circumstances "susceptible of some flexibility").

" ' "A constructive trust is the formula through which the conscience of equity finds expression. When property has been acquired in such circumstances that the holder of the legal title may not in good conscience retain the beneficial interest, equity converts him into a trustee." ' " *Brand v. Brand*, 811 F.2d 74, 77 (2d Cir. 1987) (quoting *Simonds*, 45 N.Y.2d at 241, 380 N.E.2d at 193, 408 N.Y.S.2d at 363 (1978) (quoting *Beatty v. Guggenheim Exploration Co.*, 225 N.Y. 380, 386, 122 N.E. 378, 380 (1919) (Cardozo, J.))). The doctrine's " 'applicability is limited only by the inventiveness of men who find new ways to enrich themselves unjustly by grasping what should not belong to them.' " *Simonds*, 45 N.Y.2d at 241, 380 N.E.2d at 194, 408 N.Y.S.2d at 363 (quoting *Latham*, 299 N.Y. at 27, 85 N.E.2d at 170).

Koreag contends that a constructive trust may not be imposed here because there is no confidential or fiduciary relation between the parties. We agree that no such relationship existed between Refco and Mebco. By virtue of their exchange agreements, Refco and Mebco stood in an

ordinary, arms-length commercial relationship. Purely commercial transactions do not give rise to a fiduciary relationship. *See Rodgers v. Roulette Records, Inc.*, 677 F. Supp. 731, 738-39 (S.D.N.Y. 1988); *Van Valkenburgh, Nooger & Neville, Inc. v. Hayden Publishing Co.*, 33 A.D.2d 766, 766, 306 N.Y.S.2d 599, 600 (1st Dep't 1969), *aff'd*, 30 N.Y.2d 34, 281 N.E.2d 142, 330 N.Y.S.2d 329, *cert. denied*, 409 U.S. 875 (1972).

Moreover, "[i]t is a firmly established principle that if a recipient of funds is not prohibited from using them as his own and commingling them with his own monies, a debtor-creditor, not a trust, relationship exists." *In re Black & Geddes, Inc. (Dampskibsselskabet AF 1912 Aktieselskab v. Black & Geddes, Inc.)*, 35 B.R. 830, 836 (Bankr. S.D.N.Y. 1984) (collecting cases). Here, Mebco contracted with Refco to buy and sell currencies, and was under no special duty to segregate the funds from its general account.

We do not believe, however, that the lack of a fiduciary relationship between Mebco and Refco automatically defeats Refco's claim of constructive trust. Although a fiduciary relationship is one of the factors cited by New York courts, the absence of any one factor will not itself defeat the imposition of a constructive trust when otherwise required by equity. *See Simonds*, 45 N.Y.2d at 241, 380 N.E.2d at 194, 408 N.Y.S.2d at 363; *Latham*, 299 N.Y. at 27, 85 N.E.2d at 170. New York courts have consistently stressed the need to apply the doctrine with sufficient flexibility to prevent unjust enrichment in a wide range of circumstances. *See Palazzo v. Palazzo*, 121 A.D.2d 261, 264, 503 N.Y.S.2d 381, 383-84 (1st Dep't 1986) ("the power of equity to employ a constructive trust to reach a just result is not strictly limited by the conditions set forth in *Sharp v. Kosmalski*"); *Tordai v.*

Tordai, 109 A.D.2d 996, 997, 486 N.Y.S.2d 802, 804 (3d Dep't 1985) (*Sharp v. Kosmalski* factors "are not rigid, but flexible considerations for the court to apply in determining whether a constructive trust should be imposed"); *Coco v. Coco*, 107 A.D.2d 21, 24, 485 N.Y.S.2d 286, 289 (2d Dep't 1985) (" 'these factors are merely useful guides and are not talismanic' ") (quoting *Reiner v. Reiner*, 100 A.D.2d 872, 874, 474 N.Y.S.2d 538, 541 (2d Dep't 1984)).

Hence, New York courts have at times dispensed with one or more of these requirements. In *Palazzo*, 121 A.D.2d at 264, 503 N.Y.S.2d at 383-84, for example, the court stated that the arguable lack of a transfer would not prevent the imposition of a constructive trust when the other conditions were met and equitable considerations warranted this resolution. *See also Tordai*, 109 A.D.2d at 997, 486 N.Y.S.2d at 804 (promise implied from existence of confidential relation).

More relevant to the issue at hand, the New York Court of Appeals has expressly stated that a person wrongfully acquiring property can be treated as a constructive trustee notwithstanding the lack of a fiduciary relationship. *See Simonds*, 45 N.Y.2d at 242, 380 N.E.2d at 194, 408 N.Y.S.2d at 363 (citing *Latham*, 299 N.Y. at 27, 85 N.E.2d at 170); *see also Cavallaro v. Lewis*, 198 Misc. 412, 413, 98 N.Y.S.2d 730, 731 (Sup. Ct. 1950). Further, the key factor is unjust enrichment, not willfully wrongful conduct. As the Court of Appeals stated in *Simonds*:

> It is agreed that the purpose of the constructive trust is prevention of unjust enrichment (*Sharp v. Kosmalski*, 40 N.Y.2d 119, 123, 386 N.Y.S.2d 72, 76, 351 N.E.2d 721, 724, *supra*; Restatement, Restitution, § 160; 5 Scott, Trusts [3d ed.], § 462.2).

> Unjust enrichment, however, does not require the performance of any wrongful act by the one enriched (*Lengel v. Lengel*, 86 Misc.2d 460, 465-66, 382 N.Y.S.2d 678, 681-682, *supra*; *Richards v. Richards*, 58 Wis.2d 290, 293-294, 206 N.W.2d 134, *supra*; see, generally, 5 Scott, Trusts [3d ed.], § 462.2). Innocent parties may frequently be unjustly enriched. What is required, generally, is that a party hold property "under such circumstances that in equity and good conscience he ought not to retain it" (*Miller v. Schloss*, 218 N.Y. 400, 407, 113 N.E. 337, 339; *see Sharp v. Kosmalski*, 40 N.Y.2d 119, 123, 386 N.Y.S.2d 72, 76, 351 [N.E.]2d 721, 724, *supra*; *Sinclair v. Purdy*, 235 N.Y. 245, 253-254, 139 N.E. 255, 258-259).

45 N.Y.2d at 242, 380 N.E.2d at 194, 408 N.Y.S.2d at 364.

Federal courts applying this doctrine have not been insensitive to the need for flexibility, and thus on occasion have not required a fiduciary relationship in order to impose a constructive trust. *See, e.g., E.W. Lines v. Bank of Am. Nat'l Trust Sav. Ass'n*, 743 F. Supp. 176, 179-80 (S.D.N.Y. 1990) (constructive trust imposed, applying New York law, despite absence of fiduciary relationship); *SEC v. Levine*, 689 F. Supp. 317, 321-23 (S.D.N.Y. 1988) (same), *modified on other grounds*, 881 F.2d 1165 (2d Cir. 1989); *see also Republic of Philippines v. Marcos*, 806 F.2d 344, 355 (2d Cir. 1986) ("constructive trust is simply a remedy to prevent unjust enrichment and may or may not involve a fiduciary relationship") (citing Restatement of Restitution § 160 comment a (1937)), *cert. denied*, 480 U.S. 942, 481 U.S. 1048 (1987).

We note, further, that the Disputed Funds were transferred after Mebco had been declared insolvent and

Koreag had assumed its office as liquidator of the insolvency estate under Swiss law. Such an entity is generally deemed to occupy a fiduciary status vis-a-vis creditors of the insolvency estate. *See, e.g., Commodity Futures Trading Comm'n v. Weintraub*, 471 U.S. 343, 355 (1985) (bankruptcy trustee has fiduciary duty to both creditors and shareholders); *Stein v. United Artist Corp.*, 691 F.2d 885, 892-93 (9th Cir. 1982) (debtor in possession holds title to property as fiduciary for creditors); *In re Nat'l Molding Co.*, 230 F.2d 69, 71 (3d Cir. 1956) (bankruptcy trustee, " 'as the title of his office imports, . . . *is trustee for all who have interests, and according to those interests*' ") (quoting *In re Ducker*, 134 F. 43, 47 (6th Cir. 1905) (emphasis in *Nat'l Molding*)); *Ragsdale v. New England Land & Dev. Co.*, 250 Ga. 233, ____, 297 S.E.2d 31, 32-33 (1982) (trustee in bankruptcy acts for benefit and protection of creditors).

Clearly, Koreag was acting in *some* fiduciary capacity toward *some* entities at the time it received the Disputed Funds from Refco. Whether or not this status resulted in a fiduciary relationship between Refco and Koreag for purposes of the transactions at issue and New York constructive trust doctrine, furthermore, it remains relevant to our overall assessment of the issue whether unjust enrichment has occurred for which a constructive trust should be imposed. In any event, to the extent that Koreag might be deemed to have been acting as a fiduciary for Refco, we have seen that such a relationship is not invariably required for the imposition of a constructive trust under New York law.

As to the other requirements for a constructive trust, a promise of reciprocal exchange clearly arises from the *stipulations* that, as to both types of currency exchanges at issue, "Refco and Mebco were each, at once, a pur-

chaser and seller of currencies," and "[t]he agreements between Refco and Mebco contemplated simultaneous exchanges of currencies." Further, the transfer of the Disputed Funds by Refco was manifestly made in reliance upon that promise, and the receipt of the Disputed Funds by Koreag without ultimate performance of the promised exchanges unjustly enriched Mebco's insolvency estate.

Thus, if we were to decide the issue on the present record, we would impose a constructive trust upon the Disputed Funds in behalf of Refco. The issue has not been addressed in a trial setting, however, and the definitive resolution of this essentially equitable issue should be made only after the parties have had a full opportunity to present all pertinent considerations to a finder of fact. Among other things, for example, it is at least puzzling that some currency exchanges were bilaterally performed between Refco and Mebco after Mebco went into liquidation, although those involving the Disputed Funds were not. *See supra* note 2. In any event, the question should be resolved upon a complete record.

We will therefore remand for further proceedings on this issue, not inconsistent herewith, in which Koreag will bear the practical burden, at least, of establishing why a constructive trust should not be imposed upon the Disputed Funds.

2. *New York Uniform Commercial Code.*

In the event that Refco does not prevail on the constructive trust issue, Refco's contentions regarding the New York Uniform Commercial Code (the "Code") must then be considered. Article 2 of the Code "applies to transactions in goods." N.Y.U.C.C. § 2-102 (McKinney 1964). As a threshold matter, therefore, it must be deter-

mined whether the foreign currencies that Refco and Mebco agreed to exchange were "goods" within the meaning of section 2-102.

As pertinent here, N.Y.U.C.C. § 2-105 (McKinney 1964) defines "[g]oods" as "all things . . . which are movable at the time of identification to the contract for sale *other than the money in which the price is to be paid*" (emphasis added). This definition indicates that money is excluded only when it is used as the medium of exchange. In a currency exchange contract, however, the money is not the *medium* of exchange, but rather the *object* of exchange. Such currency thus constitutes "goods" within the meaning of section 2-102, and accordingly a contract to exchange currencies is subject to the Code. This view has recently been approved by the New York Court of Appeals, which applied the Code to a contract to exchange U.S. dollars for Italian lire. *See Intershoe, Inc. v. Bankers Trust Co.*, 77 N.Y.2d 517, 521, 571 N.E.2d 641, 643, 569 N.Y.S.2d 333, 336 (1991) ("There seems no question that the UCC applies to foreign currency transactions (*see*, UCC 2-105 Official Comment 1, McKinney's Cons. Laws of N.Y., Book 62 1/2, UCC 2-105, at 96; Buerger & O'Connor, Practice Commentary, *op. cit.*, at 94).").

Since currency exchanges involve the simultaneous trading of money *qua* goods, a participant in such an exchange is both a *seller* with respect to the currency it is delivering, and a *buyer* with respect to the currency it is receiving. N.Y.U.C.C. § 2-304(1) (McKinney 1964) provides that payment under a contract can be made "in money or otherwise," and that if the price "is payable in whole or in part in goods each party is a seller of the goods which he is to transfer." Therefore, in any exchange of currencies, the parties are both sellers of the currencies

that they transfer. It follows that they are both buyers of the currencies that they receive.

Thus, Refco was at once a seller of the approximately 6.9 million dollars of the Disputed Funds that it transferred to the Account, and a buyer of the foreign currencies that the parties intended Refco to receive in exchange (the "6.9 Million Dollar Transaction"). In addition, Refco was a seller of the foreign currencies that it delivered to Mebco's European accounts from April 28 to May 2, 1989, and a buyer of the approximately 4.1 million U.S. dollars in the Account and apparently designated to pay for the transferred foreign currencies (the "4.1 Million Dollar Transaction"). The remedies available to Refco will correspond to, and vary in accordance with, Refco's respective positions as buyer and seller in the two transactions, which we address in turn.

The 6.9 Million Dollar Transaction

As a *seller* of U.S. dollars in this transaction, Refco is entitled to reclaim those dollars, whether the contract to exchange currencies is considered a sale on credit or for cash. If the transaction is deemed a credit sale, "[w]here the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days after [their] receipt." N.Y.U.C.C. § 2-702(2) (McKinney 1964). It is clear that Mebco was in fact insolvent at the time it received the U.S. dollars in question, and as will appear, Refco made appropriate demand within ten days thereafter.

If the currency exchange is considered a cash sale, Refco has a similar right of reclamation. N.Y.U.C.C. § 2-310(a) (McKinney 1964) provides that unless the parties

agree otherwise, payment for goods is due on delivery. Section 2-507(2) further specifies that "[w]here payment is due and demanded on the delivery to buyer of goods . . . , his right as against the seller to retain or dispose of them is conditional upon his making the payment due." These provisions operate to create a seller's right to reclaim goods from an insolvent buyer who takes possession of the goods, but fails to tender payment. *See Szabo v. Vinton Motors, Inc.*, 630 F.2d 1, 3 (1st Cir. 1980); *In re Samuels & Co.* (*Stowers v. Mahon*), 526 F.2d 1238, 1244-45 (5th Cir.) (in banc), *cert. denied*, 429 U.S. 834 (1976); *In re Wathen's Elevators, Inc.* (*Harris Trust & Sav. Bank v. Wathen's Elevators, Inc.*), 32 B.R. 912, 917-18 (Bankr. W.D. Ky. 1983); *see also In re Coast Trading Co.* (*Collingwood Grain, Inc. v. Coast Trading Co.*), 744 F.2d 686, 689-90 (9th Cir. 1984) (§ 2-702(2) applies to ostensible cash sales); N.Y.U.C.C. § 2-507 (McKinney 1964) official comment 3 (ten day notice requirement for reclamation under § 2-702(2) applies to § 2-507(2)).

Applying these principles, we find that Refco has a right of reclamation against Mebco with respect to the 6.9 Million Dollar Transaction. Refco's interest in the approximately 6.9 million dollars of Disputed Funds related to this transaction is therefore superior to Mebco's. Under these circumstances, these funds cannot be considered "property of [Mebco's] estate" within the meaning of 11 U.S.C. § 304(b)(2) (1988), and thus cannot be the subject of a turnover order thereunder.[7]

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7 We note that a seller's right to reclaim under N.Y.U.C.C. § 2-702(2) (McKinney 1964) "is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403)," *id.* § 2-702(3), and that a similar rule applies in the case of a constructive trust. *See Simonds*, 45 N.Y.2d at 242, 380 N.E.2d at 194, 408 N.Y.S.2d at 364; *Majer v. Schmidt*, 169 A.D.2d 501, 502, 564 N.Y.S.2d 722, 725 (1st Dep't 1991); *Birnbaum v. Birnbaum*, 117 A.D.2d 409, 420, 503

Koreag concedes that Mebco made an adequate section 2-207(2) demand for the return of those funds, but contends that Refco's state law right of reclamation is limited by 11 U.S.C. § 546(c) (1988), which provides in pertinent part:

> (c) Except as provided in subsection (d) of this section, the rights and powers of a trustee under sections 544(a), 545, 547, and 549 of this title are subject to any statutory or common-law right of a seller of goods that has sold goods to the debtor, in the ordinary course of such seller's business, to reclaim such goods if the debtor has received such goods while insolvent, but—
>
> > (1) such a seller may not reclaim any such goods *unless such seller demands in writing reclamation of such goods before ten days after receipt of such goods by the debtor*. . . .

Id. (emphasis added).

Koreag contends that § 546(c) provides the exclusive remedy for a seller who seeks to reclaim goods from a debtor in bankruptcy, *see In re Rawson Food Serv., Inc. (Flav-O-Rich, Inc. v. Rawson Food Serv. Inc.)*, 846 F.2d 1343, 1346 (11th Cir. 1988); *In re Rozel Indus., Inc. (Hitachi Denshi Am., Ltd. v. Rozel Indus., Inc.)*, 74 B.R. 643, 645 (Bankr. N.D. Ill. 1987) (collecting cases), and that Refco made only an oral demand upon Mebco (i.e., the Weiss-Savio conversation on May 3, 1989) for return of the approximately 6.9 million dollars during the ten-day period stipulated by section 546(c)(1). Mebco dis-

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N.Y.S.2d 451, 458 (4th Dep't 1986). The existence of a third party with a property interest superior to that of both the initial claimant and the debtor, however, would simply be an added reason to preclude turnover under § 304(b)(2).

counts the written demand made by Citibank upon Swiss Bank-N.Y. the same day because, Mebco contends, the relationship between Mebco (as a depositor) and Swiss Bank was that of debtor and creditor, not principal and agent. The Weiss affidavit filed in the attachment proceedings is similarly disparaged because it "did not mention Refco's alleged right to reclamation under the UCC in words or substance."

We see no merit in Koreag's position. We note that Swiss Bank-N.Y. appears clearly to have performed agency functions for Mebco with respect to the transactions at issue herein that went well beyond the "bare bones" relationship between a bank and a depositor. *See Delbrueck & Co. v. Manufacturers Hanover Trust Co.*, 609 F.2d 1047, 1051-52 (2d Cir. 1979); *Ehag Eisenbahnwerte Holding Aktiengesellschaft v. Banca Nationala A. Romaniei*, 306 N.Y. 242, 250-51, 117 N.E.2d 346, 350 (1954). In any event, § 546(c) is addressed to "the rights and powers of a trustee under sections 544(a), 545, 547, and 549 of this title," and has no bearing here.

We note in this connection that a § 304 proceeding is not a bankruptcy case that implicates the full range of procedural and substantive provisions applicable to domestic bankruptcies. *See In re Axona Int'l Credit & Commerce Ltd.*, 88 B.R. at 606 (§ 304 case does not give rise to full-scale bankruptcy with automatic stay or avoidance powers); *In re A. Tarricone, Inc.*, 80 B.R. 21, 23 (Bankr. S.D.N.Y. 1987) (§ 304 does not grant avoidance powers); *In re Meltzeler*, 78 B.R. at 677 (same); *In re Gee (Universal Casualty & Sur. Co. v. Gee)*, 53 B.R. 891, 896 (Bankr. S.D.N.Y. 1985) (§ 304 case a limited one designed to function in aid of foreign proceeding); 2 *Collier on Bankruptcy* ¶ 304.01, at 304-3 (same). Thus, the limited function of § 304 reinforces the clear language of

§ 546(c). Section 546(c) does not apply in a § 304 proceeding, and Koreag's arguments premised upon § 546(c) are accordingly unavailing.

The 4.1 Million Dollar Transaction

Refco's Code remedies with respect to this transaction are remarkably different. Here, Refco transferred foreign currencies to Mebco European accounts in anticipation of receiving corresponding U.S. dollars from the Account. Thus, Refco stands in the position of *buyer* with respect to those dollars. Accordingly, Refco has available to it only the Code remedies of a buyer, which do not include a right equivalent to that of reclamation in this case.

These remedies are set forth in N.Y.U.C.C. § 2-711 (McKinney 1964), which provides in pertinent part:

> (1) Where the seller fails to make delivery or repudiates . . . then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (Section 2-612), the buyer may cancel and whether or not he has done so may in addition to recovering so much of the price as has been paid
>
> (a) "cover" and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or
>
> (b) recover damages for non-delivery as provided in this Article (Section 2-713).
>
> (2) Where the seller fails to deliver or repudiates the buyer may also

(a) if the goods have been identified recover them as provided in this Article (Section 2-502); or

(b) in a proper case obtain specific performance or replevy the goods as provided in this Article (Section 2-716).

The official comment to this section specifies that its purpose is "[t]o index . . . the buyer's remedies, subsection (1) covering those remedies permitting the recovery of money damages, and subsection (2) covering those which permit reaching the goods themselves." *Id.* § 2-711 official comment 1. Thus, only the subsection (2) remedies could arguably provide any basis for ownership rights in specific property.

Subsection (2)(a) authorizes recovery of "identified" goods, pursuant to section 2-502. In turn, section 2-502(1) authorizes recovery of specific goods from an insolvent buyer where the goods have been identified to the pertinent contract pursuant to section 2-501. No such identification has occurred, however, in this case. Mebco was not required to provide especially identified or segregated currency, but rather any nonspecific U.S. dollars in the specified quantity.

Subsection (2)(b) authorizes specific performance or replevin as provided in section 2-716. Section 2-716(1) allows specific performance "where the goods are unique or in other proper circumstances." The U.S. dollars at issue here are obviously not "unique." The pertinent official comment states that "inability to cover is strong evidence of 'other proper circumstances.' " N.Y.U.C.C. § 2-716 (McKinney 1964) official comment 2. Similarly, section 2-716(3) authorizes replevin "for goods identified

to the contract if after reasonable effort [the buyer] is unable to effect cover for such goods." Clearly, Refco can "cover" Mebco's failure to perform its side of the 4.1 Million Dollar Transaction by obtaining other U.S. dollars.

We conclude that the Code poses no impediment to deeming the portion of the Disputed Funds that is involved in the 4.1 Million Dollar Transaction to be "property" of Mebco's estate within the meaning of § 304(b)(2). We therefore turn to Refco's alternative contention that under a proper analysis of § 304(c), turnover is inappropriate.

D. *Turnover under Section 304(c).*

Section 304(c) specifies six factors that are to be considered in fashioning a remedy in an ancillary case, including turnover of property. Four of those factors are relevant to this case:

> (1) just treatment of all holders of claims against or interest in such estate;
>
> (2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;
>
> . . . .
>
> (4) distribution of proceeds of such estate substantially in accordance with the order prescribed by this title; [and]
>
> (5) comity . . . .

11 U.S.C. § 304(c) (1988).

Further, as noted earlier, the overriding purpose of § 304 is to prevent piecemeal distribution of a debtor's estate, and a bankruptcy court is accorded broad latitude

in fashioning an appropriate remedy in a § 304 proceeding.

Refco argues that under the relevant § 304(c) factors, turnover of the property was improper because the bankruptcy court improperly emphasized the factor of "comity" to the exclusion of other vital considerations. Although neither the Code nor the legislative history accords superior weight to the comity factor, the bankruptcy court deemed itself bound by prior Southern District of New York decisions holding that comity is of paramount concern. *See Koreag*, 130 B.R. at 712 (citing *In re Culmer*, 53 B.R. at 628; *In re Gee*, 53 B.R. at 891). *But see In re Papeleras Reunidas, S.A.*, 92 B.R. 584, 594 (Bankr. E.D.N.Y. 1988) (comity given only equal weight with other factors; Southern District view explicitly rejected).

We see no need to reconcile these disparate views in the present posture of this case. If Refco prevails on the constructive trust issue upon remand, none of the Disputed Funds will be subject to turnover. If Koreag prevails on that issue, only the portion of the Disputed Funds involved in the 4.1 Million Dollar Transaction will be subject to turnover. Under any view of the relative weight to be accorded the pertinent § 304(c) factors, turnover would be a permissible exercise of discretion as to those funds.

In the only possible turnover scenario, the funds subjected to turnover would be subject only to Refco's claim as a general, unsecured creditor. Refco could assert no valid security interest or other benefit of domestic law whose deprivation might render a turnover unfair or otherwise improper. *Cf. Interpool, Ltd. v. Certain Freights of the M/V Venture Star*, 102 B.R. 373, 378-80 (D.N.J. 1988)

(denying § 304 petition because American creditor denied procedural protections and remedy of equitable subordination under Australian law), *appeal dismissed*, 878 F.2d 111 (3d Cir. 1989); *In re Toga Mfg. Ltd.*, 28 B.R. 165, 168-71 (Bankr. E.D. Mich. 1983) (denying § 304 petition because domestic creditor would lose priority status in Canadian proceeding).

As the bankruptcy court stated, "Refco does not dispute that Switzerland's insolvency procedures are fundamentally fair." *Koreag*, 130 B.R. at 715. Accordingly, Refco will not be prejudiced if required to litigate unsecured claims in a Swiss proceeding. Comity calls for such a result, and Refco's prior attachment of the Disputed Funds does not suffice to defeat a turnover order under § 304(c). *See Cunard*, 773 F.2d at 458.

Conclusion

The revised order of the district court is vacated and the matter is remanded for further proceedings not inconsistent with this opinion. The order of this court entered October 1, 1991 that granted a stay pending final determination of this appeal is continued, pending final determination of the § 304 proceeding upon remand. Any future appeal in that proceeding shall be referred to this panel. The mandate shall issue forthwith.

UNITED STATES COURT OF APPEALS
Second Circuit
United States Courthouse
Foley Square
New York 10007

ELAINE B. GOLDSMITH
Clerk

DATE: April 9, 1992
Re: Koreag v. Refco F/X
Docket No.(s): 91-5061

Dear Counsel:

The court has handed down a decision in the above-entitled case. The decision of the district court has been vacated and remanded. Mandate shall issue forthwith.

A copy of the printed opinion will be mailed to you. Additional copies of the opinion may be obtained from this office in accordance with Section 0.17 (7) of the rules of this court supplementing the Federal Rules of Appellate Procedure.

Judgment has been entered today and a mandate will issue in accordance with Rule 41 of the Federal Rules of Procedure.

Your attention is directed to the Provision of Rule 39(c) of the Federal Rules of Appellate Procedure requiring the itemized and verified bill of costs, if any, to be filed with proof of service, within 14 days after entry of judgment.

Very truly yours,

ELAINE B. GOLDSMITH, Clerk
By: L. DOBBS

/s/ L. DOBBS
Deputy Clerk

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pc/opn/f

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Docket No. 91-5061

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 9th day of April, one thousand nine hundred and ninety-two.

Present: HON. GEORGE C. PRATT,
HON. J. DANIEL MAHONEY,
HON. JOSEPH M. MCLAUGHLIN,
Circuit Judges.

KOREAG, CONTROLE et REVISION S.A.,

Petitioners-Appellee,

—against—

REFCO F/X ASSOCIATES, INC.,

Respondent-Appellant.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged and decreed that the order of said district court be and it hereby is vacated and the action be and it hereby is remanded to the district court for further proceedings not inconsistent with the opinion of this court. The *Order* of this court entered October 1, 1991 that granted a stay pending

final determination of this appeal is continued, pending final determination of the § 304 proceeding upon remand in accordance with the opinion of this court.

ELAINE B. GOLDSMITH, Clerk
By:

Edward J. Guardaro
Staff Attorney

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

89 CIV. 3071 (WK)

REFCO F/X ASSOCIATES, INC.,

Plaintiff,

—against—

MEBCO BANK, S.A.,

Defendant.

Appearances

For Plaintiff:

JACK WEINBERG, ESQ.
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MEMORANDUM & ORDER

WHITMAN KNAPP, D.J.

This action arises out of defendant Mebco Bank's failure to perform its side of currency transactions entered into with plaintiff Refco F/X Associates. Plaintiff obtained *ex parte* an order attaching defendant's account at Swiss Bank Corpora-

tion's New York branch. Now before us are plaintiff's motion to confirm that attachment and defendant's cross-motion to dismiss the complaint.

Defendant seeks dismissal on three grounds: (1) pursuant to Fed. R. Civ. P. 12(b)(3) on *forum non conveniens* grounds; (2) pursuant to Fed. R. Civ. P. 12(b)(1) asserting that the attachment should be vacated on the grounds of comity, and that, absent the attachment, the amended complaint fails to allege personal jurisdiction over the defendant; and (3) pursuant to Fed. R. Civ. P. 12(b)(6) on the ground that principles of comity require resolution of plaintiff's claims in Switzerland.

For reasons that follow, we deny defendant's motion to dismiss for *forum non conveniens*. With respect to the other grounds asserted, the motion is denied without prejudice to defendant's seeking relief by means of a § 304 application to the bankruptcy court on or before December 27.

BACKGROUND

Plaintiff Refco F/X Associates, Inc., a New York corporation with its principal place of business in New York, trades in commodities and currencies. From June 1988 until April 1989, through its London office it entered into currency exchange transactions with defendant Mebco Bank, a Swiss banking corporation with its principal place of business in Geneva. Pursuant to these transactions, the parties purchased foreign currency from each other in exchange for U.S. dollars.

Each currency transaction was accomplished in two stages. First the parties agreed upon an exchange and set a settlement date. Then, on the settlement date, usually several days later, the exchange was accomplished by simultaneous wire transfers. Defendant maintained a New York bank account—now subject to attachment—through which, depending on the transaction, it either paid U.S. dollars to plaintiff or collected them from plaintiff U.S. dollars.

BEST AVAI

This dispute involves various transactions which were to be executed on or after April 27, the date the Swiss Banking Commission placed defendant in liquidation and revoked its banking license. Apparently unaware of the Commission's actions, plaintiff transferred funds to the defendant's New York and foreign accounts in performance of its side of these transactions. Defendant allegedly failed to return performance.

In its complaint, plaintiff demands the return of the funds that it deposited in defendant's account at Swiss Bank and the U.S. dollar equivalent of the foreign currencies for which it has not received payment. Plaintiff asserts that the liquidator instructed all banks holding funds for the defendant not to pay out without also instructing them not to accept funds paid in. Thus, plaintiff contends, defendant accepted performance of transactions knowing it could not return performance.

This contention presents a rather complicated question of fact. Notwithstanding its allegation that the liquidator instructed banks not to make payments on defendant's behalf, Am. Complt. ¶ 24, plaintiff asserted at oral argument that it was the Swiss Banking Commission rather than the liquidator that froze defendant's accounts, Tr. at 6-7. In contrast, the account officer in charge of defendant's New York Swiss Bank account claims that, after learning that defendant's banking license had been revoked, he gave the instructions to stop payments out of defendant's account. Ernest Kung Affid. at ¶ 5.

DISCUSSION

Defendant's motion to dismiss for *forum non conveniens* merits only brief discussion. In support of its contention that Switzerland is the more convenient forum, defendant asserts that it "ha[s] nothing to do this forum." We disagree. It maintains a bank account in New York through which all of its transactions with the plaintiff were accomplished. The bank records indicating defendant's payment orders and

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plaintiff's deposits presumably will be of considerable evidentiary value as will the testimony of the bank's officers who allegedly received instructions from the liquidator to withhold payment of funds but were never told not to accept funds on defendant's behalf. Moreover, the funds, to which plaintiff claims a right of reclamation, are here, not in Switzerland. Additionally, we note that plaintiff is a New York corporation with its principal place of business here. In short, defendant has not met its burden of demonstrating that the Southern District of New York would be an inconvenient forum and that plaintiff should be required to pursue its claims in Switzerland.

We turn now to the remaining grounds for defendant's motion to dismiss as well as plaintiff's motion to confirm the attachment. To determine whether to confirm the attachment, we must consider the likelihood of plaintiff's success on the merits, *see Deutsche Anlagen-Leasing* v. *Kuehl* (1st Dep't 1985) 489 N.Y.S.2d 195, 197, which may well turn on the merit of defendant's contention that we should defer to the Swiss proceedings. The decision whether to defer to the foreign proceedings necessarily involves an evaluation of them. *See, e.g., Drexel Burnham Lambert Group Inc.* v. *Galadari* (2d Cir. 1985) 777 F.2d 877; *In re Axona Int'l Credit & Commerce Ltd.* (Bankr. S.D.N.Y. 1988) 88 B.R. 597.

We conclude that evaluation of the Swiss proceedings should be conducted in the context of a proceeding instituted in the bankruptcy court pursuant to 11 U.S.C. § 304. Defendant, citing *Cunard Steamship Co.* v. *Salen Reefer Services* (2d Cir. 1985) 773 F.2d 452, argues that a § 304 proceeding is not the exclusive remedy of a bankrupt's foreign representative who wishes to stay or enjoin creditor actions in the United States. However, we note that, in *Cunard*, the Second Circuit found that a § 304 proceeding is the *preferred* remedy, recognizing that "[t]he bankruptcy courts' expertise in bankruptcy matters should prove helpful in appraising foreign bankruptcy proceedings and in determining the effect those proceedings should be given in the United States." *Id.* at 455, 461.

We conclude that § 304 was designed for cases such as this one, and therefore deny the motion to dismiss the complaint with respect to the second and third grounds asserted without prejudice to defendant's seeking relief by means of a § 304 application to the bankruptcy court. Should no such application be made by Wednesday, December 27 (unless an extension of time shall have been granted), the motion to confirm the attachment will that day be granted.

Dated: December 11, 1989
New York, New York

WHITMAN KNAPP U.S.D.J.

[THE DATE OF ENTRY OF THIS DECISION DOES NOT APPEAR ON THE COURT'S DOCKET.]

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

Case No. 90-B-10037 (CB)

In Re:

KOREAG, CONTROLE et REVISION S.A., as Official Liquidator of MEBCO BANK, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

BEFORE:

HON. CORNELIUS BLACKSHEAR,
Bankruptcy Judge.

DECISION ON PETITION FOR RELIEF ANCILLARY TO FOREIGN PROCEEDING UNDER SECTION 304 OF THE BANKRUPTCY CODE AND FOR A PRELIMINARY INJUNCTION

This matter comes to this Court by way of section 304 of the Bankruptcy Code (the "Code") pursuant to which an ancillary proceeding was filed by the Koreag, Controle et Revision S.A. (the "Petitioner") as the Official Liquidator of Mebco Bank, S.A. ("Mebco"), a foreign corporation organized and existing under the laws of Switzerland. Refco F/X Associates, Inc. ("Refco"), a corporation organized and existing under the laws of New York with its principal place of business in New York City, has filed (1) opposition to Petitioner's motion for relief under the Code and for a preliminary injunction and (2) a cross-motion, pursuant to Rule

12(b), Fed. R. Civ. P., and Bankruptcy Rule 1011, to dismiss the petition.

On May 5, 1989, Refco commenced an action against Mebco in the United Sates District Court for the Southern District of New York, *Refco F/X Associates Inc. v. Mebco Bank, S.A.*, 89 Civ. 3071 (WK) (the "District Court Action"). Refco also obtained an *ex parte* order of attachment against Mebco's bank account at Swiss Bank - N.Y. In the District Court Action, Refco made a motion to confirm the order of attachment and Mebco cross-moved to dismiss the complaint. The district court denied Mebco's motion to dismiss for *forum non conveniens*. The district court also denied Mebco's motion to dismiss on other grounds, without prejudice to seeking relief by means of a section 304 petition to this Court. The district court stated that if Mebco did not file such a petition, Refco's motion to confirm the attachment would be immediately granted. On January 5, 1990, the Petitioner filed the instant petition seeking relief pursuant to section 304, together with a motion to enjoin Refco's prosecution of the District Court Action.

FACTS

Refco is a dealer in foreign currencies, including forward, spot contracts and options thereon. Mebco is not qualified or authorized to do business in the State of New York. Stip. at ¶ 2.[1] Before its liquidation, Mebco engaged in the banking business and, in the course of such business, dealt in foreign currencies for its own account. Stip. at ¶ 4.

In May 1986, a representative from Refco's London Office met with an officer of Mebco at Mebco's sole office in Geneva to discuss a potential trading relationship. Stip. at ¶ 6. Subsequent contacts between Mebco and Refco's London office took place exclusively in Europe. Stip. at ¶ 9. In 1987, pursuant to Refco's request, Mebco presented to Refco

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1 The Stipulation of Facts dated September 14, 1989 (Exhibit 3), between Refco and Mebco will be referred to as "Stip."

its annual audited financial statement, dated December 31, 1986. Subsequently, Refco requested and received Mebco's annual report for 1987. Stip. at ¶ 6.

Refco and Mebco began trading currencies with each other in June 1988, when Refco extended to Mebco a $10 million line of credit. Stip. at ¶ 8. Refco continued to rely on Mebco's financial statements during Refco's ongoing business relationship with Mebco. Weiss Aff. at ¶ 6.

Between June and April 1989, Refco and Mebco conducted business on a daily basis, sometimes conducting as many as five currency transactions in a single day. Stip. at ¶ 10. Between April 20, 1989 to April 27, 1989, Refco and Mebco entered into various agreements to exchange currency as they had done in the past. Stip. at ¶ 17. These agreements contemplated that the purchases and sales of currencies would be simultaneous transactions. Stip. at ¶ 16. The transactions were twofold: (1) Refco delivered into the Mebco general account at Swiss Bank - N.Y., $6.9 million U.S. dollars and, in exchange, Refco was to receive from Mebco foreign currencies of comparable value; and (2) Refco was to receive from Mebco more than $4 million U.S. dollars in exchange for foreign currencies that Refco delivered to Mebco. The foreign currency side of the transactions was to take place at various banks in Europe. The U.S. dollar side of the transactions was to be effected through Mebco's general account at Swiss Bank - N.Y. Stip. at ¶ 5, 14, 15; Weiss Aff. at ¶ 6.

On April 27, 1989, at 10:15 a.m. (EST), Switzerland's Federal Banking Commission placed Mebco into liquidation. Stip. at ¶ 18. At 11.00 a.m. (EST), petitioner was appointed the Official Liquidator of Mebco by the Federal Banking Commission in Switzerland. Stip. at ¶ 19.

Following the decision to place Mebco into liquidation and the appointment of Petitioner as Official Liquidator of Mebco, a public announcement was made in Switzerland alerting the financial and investing public of these events. Levy Aff. at ¶ 3. This information was reported almost immediately by the Dow Jones International News Service and later by *The Financial Times*. Stip. at ¶ 20.

Shortly thereafter, at 3:46 p.m. (EST), Refco wire transferred funds into Mebco's account at Swiss Bank - N.Y. Stip. at ¶¶ 21 and 22. At 3:52 p.m. the following day, April 28, 1989, Refco made yet another deposit. Stip. at ¶ 22. Mebco delivered some foreign currencies to Refco, but failed to deliver foreign currencies against $6.9 million of the U.S. dollars that Refco had sold to Mebco and deposited at Swiss Bank - N.Y. Stip. at ¶ 22; Weiss Aff. ¶ 9.

On April 27, 1989, at approximately 2:00 p.m. (EST), Mebco's account officer at Swiss Bank, Ernest Kung ("Kung"), read over the Dow Jones International News Service that the Swiss Banking Commission revoked Mebco's banking license. Kung Aff. at ¶ 5. Kung immediately stopped all of Mebco's payment orders to Refco. Kung Aff. at ¶ 5. The next day, April 28, 1989, Swiss Bank received a telex from Swiss Bank Corporation in Geneva (a) advising that Mebco's license was revoked by the Swiss Banking Corporation, (b) directing that Swiss Bank immediately stop working with Mebco, and (c) notifying Swiss Bank that all Mebco accounts had been blocked and that no other commitments were to be taken. Stip. at ¶ 23; Kung Aff. at ¶ 7.

There is in excess of $12.5 million in Mebco's Swiss Bank - N.Y. account.[2] This represents deposits, amounting to millions of dollars, from Mebco creditors in addition to Refco. Mebco currently has over 400 creditors around the world.

On May 3, 1989, Gary Weiss ("Weiss") of Refco telephoned Mebco in Geneva, Switzerland. Stip. at ¶ 26. Weiss's call was referred to a Mr. Savio who claimed that Mebco's accounts had been frozen and that his company, Koreag, had been named "liquidator." Stip. at ¶ 27. Savio also told Refco that (i) Mebco's Geneva banking license had been revoked by the Swiss Banking Commission at 11:00 a.m. (EST) on April 27, 1989, and (ii) at that time, his company was appointed as "liquidator." Stip. at ¶ 27; Weiss Aff. at ¶ 14. Savio also told Weiss that Mebco's side of the open transactions with Refco would not be completed. Stip. at

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2 This figure is not the most current since the amount of funds in Mebco's Swiss Bank - N.Y. account may have increased since the time the briefs were submitted and the hearing was conducted.

¶ 31; Weiss Aff. at ¶ 16. Weiss demanded that Mebco immediately return to Refco the U.S. dollars and foreign currencies that Refco deposited into Mebco's accounts. Stip. at ¶ 29.

On May 3, 1989, Citibank - N.Y., on behalf of Refco, sent a telex message to Swiss Bank - N.Y., demanding the return of $7,407,510 that Refco deposited into Mebco's account at Swiss Bank on April 27, 1989. Stip. at ¶ 33. On May 3, 1989, Citibank - N.Y., on behalf of Refco, sent a telex message to Swiss Bank - N.Y., demanding the return of $2,000,000 that Refco deposited into Mebco's account at Swiss Bank - N.Y. Stip. at ¶ 34.

On January 5, 1990, the Petitioner filed the instant petition seeking relief pursuant to § 304, together with a motion to, *inter alia*, enjoin Refco's prosecution of the District Court Action and to direct turnover of all the funds in Mebco's Swiss Bank - N.Y. account to the Petitioner for administration in the Swiss Proceedings. Refco, in rebuttal, objects to the injunctive relief requested by the Petitioner and to the turnover of Mebco's assets. Additionally, Refco seeks to dismiss the § 304 petition.

DISCUSSION

Section 304 of the Code authorizes a representative appointed in a foreign bankruptcy proceeding to file a petition in the United States Bankruptcy Court ancillary to the foreign proceeding. The fundamental purpose of section 304 is to afford the foreign bankrupt the opportunity to "prevent the piecemeal, distribution of [its] assets [located] in this country . . ." by local creditors. *Victrix Steamship Co. S.A. v. Salen Dry Cargo A.B.*, 825 F.2d 709, 713-14 (2d Cir. 1987); *accord Cunard Steamship Co. Ltd. v. Salen Reefer Service, A.B.*, 773 F.2d 452, 453-54 (2d Cir. 1985); *In re Lines*, 81 B.R. 267 (Bankr. S.D.N.Y. 1988).

A § 304 filing, however, does not create a full scale bankruptcy case with the protections of an automatic stay or with the Code's avoiding powers. H.R. Rep. No. 95-595, 95th

Cong., 1st Sess. 324-25 (1977); S.Rep. No. 95-989, 95th Cong., 2nd Sess. 35 (1978), U.S. Code Cong. & Admin. News 1978, 5787, 5821, 6280, 6281. *See also*, *Matter of Axona Int'l Credit & Commerce, Ltd.*, 88 B.R. 597, 606 (Bankr. S.D.N.Y. 1988); *Universal Casualty & Surety Co., Ltd. v. Gee (In re Gee)*, 53 B.R. 891, 896 (Bankr. S.D.N.Y. 1985); *In re Trakman*, 33 B.R. 780, 783 (Bankr. S.D.N.Y. 1983); *Matter of Culmer*, 25 B.R. 621, 624 (Bankr. S.D.N.Y. 1982).

Instead, a § 304 petition creates a bankruptcy case limited in scope and designed to aid in the foreign proceedings. *Matter of Axona*, 88 B.R. at 606.

The limited scope of a § 304 petition, however, is balanced with the broad powers granted the bankruptcy court in determining the type of relief to be granted the § 304 petitioner. The bankruptcy court may:

> (1) enjoin the commencement or continuation of
>
> (A) any action against
>
> (i) a debtor with respect to property involved in such foreign proceeding; or
>
> (ii) such property; or
>
> (B) the enforcement of any judgment against the debtor with respect to such property, or any act on the commencement on continuation of any judicial proceeding to create or enforce a lien against the property of such estate;
>
> (2) order turnover of the property of such estate, or the proceeds of such property, to such representative; or
>
> (3) order other appropriate relief.

11 U.S.C. § 304(b).

The powers of the bankruptcy court in a § 304 context have been described as giving the Court the ability to "mold relief in near blank check fashion. . . ." *Matter of Culmer*, 25 B.R. at 624. In making a determination as to the type of relief to grant, the bankruptcy court "shall be guided by what will best assure an economical and expeditious adminis-

tration of such estate." 11 U.S.C. § 304(c). Section 304(c) sets forth six factors to be taken into account when fashioning the appropriate relief in a § 304 petition that will accomplish an economical and expeditious administration of the bankrupt's estate.

It is apparent that Congress, in allowing the bankruptcy court flexibility in the exercise of the § 304 powers, recognized that transnational bankruptcies give rise to a "multitude of complex and unforseen problems. . . ." *In re Gee*, 53 B.R. at 896-897; H.R. Rep. No. 595, 95th Cong., 1st Sess., 324-25 (1977), S.Rep. No. 989, 95th Cong., 2d Sess., 35, 1978, U.S. Code Cong. & Admin. News 5963, 6281.

Jurisdiction

Refco's threshold argument is jurisdictional. It claims that this Court lacks subject matter jurisdiction under § 304 because under the Code and the laws of New York, the attached funds are neither part of Mebco's estate nor property of Mebco. The following are the legal theories upon which Refco relies:

(a) Refco properly and timely exercised its rights under the U.C.C. to cancel its currency exchange agreements and reclaim its money;

(b) Refco was defrauded by Mebco's misrepresentation of its financial condition when Refco agreed to the currency exchanges and when Refco made the payments at issue here;

(c) Refco's money is impressed with a constructive trust in favor of Refco because the money was obtained wrongfully, and Mebco and its creditors would be unjustly enriched if the liquidation were permitted to retain Refco's funds; and

(d) when the Swiss liquidation proceeding was commenced, the currency exchange agreements between Refco and Mebco were executory. Even if Refco's funds (which were delivered after the liquidator's appointment) were deemed a part of Mebco's

> "estate" or Mebco's property at the time of delivery, Refco's funds cannot be retained by the liquidation without performing Mebco's side of the transaction.

All that a foreign representative need do to invoke the bankruptcy court's jurisdiction under section 304 is allege that: (1) a foreign proceeding was commenced against the debtor; (2) the petitioner is a foreign representative entitled to file the action under section 304; and (3) the debtor had certain assets within the judicial district where the petition was filed."[3] *In re Trackman*, 33 B.R. at 783. *See also Metzeler v. Bouchard Transp. Co. Inc. (In re Metzeler)*, 78 B.R. 674, 678-79 (Bankr. S.D.N.Y. 1987); *Strelittz v. Stuppel (Matter of Stuppel)*, 17 B.R. 413, 415 (Bankr. S.D.Fla. 1981).

A foreign representative is defined in § 101(23) of the Code to mean a "duly selected trustee, administrator, or other representative of an estate in a foreign proceeding." 11 U.S.C. § 101(23). Clearly, the Petitioner is a foreign representative falling within the scope of this definition. It is undisputed that under Swiss law, "once a bank is placed into liquidation, the Banking Commission appoints a liquidator to administer the bank's assets and to act for the bank in all areas." Stip. at ¶ 9.

A foreign proceeding is one which is either judicial or administrative in a "foreign country in which the debtor's domicile, residence, principal place of business or principal assets were located at the commencement of such proceeding, for the purpose of liquidating an estate, adjusting debts by composition, extension, or discharge, or effecting a reorganization." 11 U.S.C. § 101(22). The proceedings in Switzerland, where Mebco's principal place of business is located, are liquidation proceedings clearly falling within the definition of a foreign proceeding. Stip. at ¶ 1.

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3 Controversy exists as to whether this last requirement must be satisfied in order to establish jurisdiction. *In re Metzeler*, 78 B.R. 674. However, that is not an issue before this Court and therefore is not considered in this decision.

This § 304 petition also satisfies the last requirement, that the debtor have assets within the judicial district where the § 304 petition was filed. Mebco has a bank account in Swiss Bank - N.Y. containing $12.5 million. Refco claims that pursuant to the Code and the laws of New York, the attached funds, totalling $6.9 million, cannot constitute part of Mebco's estate subject to this Court's jurisdiction. In taking this position, Refco is placing the proverbial "cart before the horse." Section 304(c) allows the bankruptcy court to turnover assets located locally to the foreign representative, thereby subjecting local creditors to the laws of the foreign tribunal. It is axiomatic that if a local creditor is forced to have its rights adjudicated in a foreign forum, that creditor will not enjoy the same rights that it would otherwise enjoy in an American case. The inherent question faced by all courts when asked to turnover assets in a § 304 proceeding is whether the rights of its local creditors should be determined pursuant to American jurisprudence or whether the interests of justice would be better served if the local creditor were subjected to the laws of a foreign country in the context of the foreign proceeding. By arguing that pursuant to the Code and the laws of New York this Court lacks subject matter jurisdiction over the attached funds because they are not part of Mebco's estate, Refco's underlying assumptions are that the petitioner's turnover request will be denied, Refco will not be forced to participate in the Swiss liquidation proceedings and that Refco's claim will be adjudicated in an American court. Refco's contentions that the funds in the Swiss Bank - N.Y. are subject to attachment goes to this Court's consideration of the Petitioner's turnover request not to the jurisdictional issue.

Therefore, when conducting a jurisdictional analysis, the laws in the foreign proceeding are determinative of whether the foreign bankrupt has assets located in the district in which the § 304 petition was filed. *Matter of Toga Mfg., Ltd.*, 28 B.R. 165, 167 (Bankr. E.D. Mich. 1983) (Wherein the court looked to the bankruptcy laws of the foreign country to determine whether property located in the United States was part of the foreign bankrupt's estate) (cited in *In*

re Metzeler, 78 B.R. at 677); *see also Matter of Axona*, 88 B.R. at 599 (the court's 304 jurisdiction was invoked where foreign bankrupt had bank accounts located in New York which had been attached by local creditors). Under Swiss law, the funds in Mebco's bank account at Swiss Bank - N.Y. are included in the property involved in Mebco's liquidation proceedings. Levy Aff. ¶ 3. The last jurisdictional requirement is satisfied since the funds are located in this district.

The § 304(c) Factors

The Petitioner seeks an order enjoining the continuation of the District Court Action; enjoining the commencement of any actions against Mebco or its property located in this district; enjoining the attachment or garnishment and the creation, perfection and enforcement of any lien, setoff or other claim against any asset of Mebco located within this district; and directing that all assets held for the account of Mebco and all monies or other assets located in this district which are now due or which hereafter may become due to Mebco be turned over to the Petitioner.

The six § 304(c) factors are:

(1) just treatment of all holders of claims against or interest in such estate;

(2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;

(3) prevention of preferential or fraudulent disposition of property of such estate;

(4) distribution of proceeds of such estate substantially in accordance with the order prescribed by this title;

(5) comity; and

(6) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

11 U.S.C. § 304(c).

The gravamen of the issues before this Court is the proper weight that should be accorded "comity", the fifth enumerated factor. Refco correctly points out that neither § 304(c) nor its legislative history explicitly provide that comity should be afforded more weight than the other factors. The bankruptcy court in this district, however, views comity as a significant factor in the application of § 304(c). Judge Lifland, in *Matter of Culmer*, 25 B.R. 621 (Bankr. S.D.N.Y. 1982), stated that "[a]ll of the factors listed in section 304(c) have historically been considered within a court's determination whether to afford comity to a proceeding in a foreign nation." *Id.* at 629. Similarly, Judge Brozman, in *In re Gee*, 53 B.R. 891 (Bankr. S.D.N.Y. 1985), stated that comity will usually "be the most significant [factor] where it serves as the crux of the debtor's argument." 53 B.R. at 891. This district is not alone in its assessment of the significance of comity. *See Interpool, Ltd. v. Certain Freights of M/V Venture Star*, 102 B.R. 373, 377 (D.N.J. 1988) (where the court cited *In re Gee*). This view is not is without opposition and criticism. *See Matter of Papeleras Reunidas, S.A.*, 92 B.R. 584, 594 (Bankr. E.D.N.Y. 1988) (the bankruptcy court, in flatly rejecting the view of the bankruptcy court in this district, gave equal weight to comity). This Court is compelled to follow the lead of *Matter of Culmer* and *In re Gee*. While it is true that neither the Code nor its legislative history explicitly require that comity be afforded more weight than the other 304(c) factors, neither does it provide that all of the factors must be given equal weight. Comity is inevitably the more significant factor since the other factors (except for the sixth element dealing with the fresh start theory) are inherently taken into account when considering comity. *Matter of Culmer*, 25 B.R. at 629.

The often cited definition of comity is:

> The recognition which one nation allows within its territory to the legislative, executive, on judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citi-

zens or of other persons who are under the protection of its laws.

Hilton v. Guyot, 159 U.S. 113, 164, 16 S.Ct. 139, 143, 40 L.Ed. 95 (1895); *Cunard Steamship Co.*, 773 F.2d at 456; *Matter of Culmer*, 25 B.R. at 629.

The mere filing of a § 304 petition does not automatically require that the local bankruptcy court grant comity to the foreign court. Instead the bankruptcy court must make a case-by-case determination. Comity shall be granted where it has been demonstrated that the foreign court is a court of "competent jurisdiction, and that the laws and public policy of the forum state and the rights of its residents will not be violated." *Cunard Steamship Co.*, 773 F.2d at 457; *In re Gee*, 53 B.R. at 901. This Circuit recognizes that the general principals of comity as well as the provisions of § 304 require recognition of foreign bankruptcies where the foreign bankruptcy proceedings "comport with due process and fairly treat claims of local creditors." *Victrix Steamship*, 825 F.2d at 714; *see also*, *Banque de Financement S.A. v. First Nat. Bank of Boston (Banque de Financement)*, 568 F.2d 911, 921 (2d Cir. 1977). And when examining all of the 304(c) factors, the focus of the bankruptcy court is "whether the relief petitioner[ ] seek[s] will afford equality of distribution of the available assets." *Matter of Culmer*, 25 B.R. at 628 (cited in *In re Banco Nacional de Obras y Servicios Publicos*, 91 B.R. 661, 667 (Bankr. S.D.N.Y. 1988) (court stated that comity "will not be granted in the bankruptcy context if it would result in forcing American creditors to participate in foreign proceedings in which their claim will be treated in some manner inimical to this country's policy of equality")). Naturally, comity shall not be granted where, by doing so, the local court is approving of a transaction that is "vicious, wicked or immoral, and shocking to the prevailing moral sense." *Intercontinental Hotels Corp. v. Golden*, 254 N.Y.S.2d 527, 529 (1964) (quoted in *Cornfeld v. Investors Overseas Services, Ltd.*, 471 F. Supp. 1255, 1259 (S.D.N.Y. 1979)).

The purpose of granting comity to foreign bankruptcy proceedings is quite simple and very logical. Essentially, section

304 reflects the notion that it is in the best interests of a foreign debtor and its entire creditor body to disperse the assets of that debtor, wherever located, "in an equitable, orderly, and systematic manner, rather than in a haphazard, erratic or piecemeal fashion." *Cunard Steamship Co.*, 773 F.2d at 458; *Victrix Steamship*, 825 F.2d at 714 (court spoke to the "public policy of ensuing equitable and orderly distribution of local assets of a foreign bankrupt"). Given the stated purpose of the doctrine of comity and of § 304, when determining whether to suspend this 304 proceeding and turnover the attached funds to the Petitioner to allow the assets to be administered in the Swiss proceeding, this Court must consider not only the treatment Refco would be afforded under Swiss law, *i.e.*, the procedural fairness of the Swiss law, but also determine what will result in the efficient and economical administration of Mebco's pending Swiss bankruptcy proceeding. This, of course, is the inherent tension found within the section 304(c) factors. If, however, the "foreign law is not repugnant to our own the scale will ordinarily tip in favor of having the foreign tribunal liquidate claims against the estate, because the equitable and orderly distribution of the debtor property can best be accomplished in a single proceeding." *In re Banco Nacional de Obras y Servicios Publicos*, 91 B.R. at 667.

Refco argues against turnover of the attached funds to the Swiss proceeding because its claim will not be treated the same as if it were adjudicated in the United States. Specifically, Refco claims that under the Code and the laws of New York, its claim to the attached funds would enjoy secured status whereas under the laws of Switzerland, its claims would be relegated to the status of an unsecured creditor.[4] This Court need not address the merits of Refco's claim that under the Code and New York laws it holds a secured claim

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4 It is undisputed that under the laws of Switzerland, Refco would be treated as an unsecured creditor.

because that is not the test under section 304.[5] The test is whether the proceedings in Switzerland comport with fundamental notions of fairness, *Matter of Banque de Financement, S.A.*, 568 F.2d at 921, not that the foreign bankruptcy laws are a mirror image of our own. *In re Gee*, 53 B.R. at 904; *Matter of Axona*, 88 B.R. at 610-11 ("whether or not Hong Kong law is identical to American law, Hong Kong law is not repugnant to our ideas of justice, and is inherently fair and regular"); *see also Daniels v. Powel*, F. Supp. 689, 693 (N.D. Ill. 1985) (the mere fact that the foreign law is not identical is insufficient to deny comity). An examination of the § 304(c) factors will assist this Court in reaching such a determination.

In its support, Refco relies on the holdings in *Matter of Toga*, 28 B.R. 165 (Bankr. E.D.Mich. 1983) and *Matter of Papeleras*, 92 B.R. 584 (Bankr. E.D.N.Y. 1988). This Court, however, disagrees with the respective holdings in those cases.

The bankruptcy court in *Toga* refused to turnover the assets located in its district to the Canadian court to be administered in the Canadian bankruptcy proceeding where the local creditors would not enjoy under Canadian law the same secured status they would enjoy in the United States. *Toga*, 28 B.R. at 170. Indeed the facts in *Toga* are strikingly similar to those before this Court. However, the reasoning of the court in *Toga* has been criticized as protectionist. In a more recent decision, Judge Lifland noted that in the court's limited focus on affording the U.S. creditor the same rights it enjoyed under U.S. laws, prevented the court "from considering the full scope and procedural fairness of Canadian law." *Matter of Axona*, 88 B.R. at 611. (citing, Note, Section 304 of the Bankruptcy Code; Has it Fostered the Development of an "International Bankruptcy System," Colum. J. Transnat'l L. 541, 566 (1984)).

The facts in *Matter of Papeleras* are altogether different than those before this Court. In *Papeleras*, the bankruptcy court refused to require the local creditor to have its claim

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5 The remainder of this decision will proceed on the assumption that Refco's claim is entitled to a secured status pursuant to the Code and New York laws.

satisfied in a Spanish court. The court in *Papeleras* held that the local creditor would not be afforded just treatment in the Spanish proceeding because under Spanish law, only liquidated claims are recognized and the local creditor held a disputed claim at the time the Spanish proceedings commenced. *Papeleras*, 92 B.R. at 590. The local creditor's claim was not recognized under Spanish law until it had been liquidated by a determination by a United States Circuit Court of Appeals by which point most of the assets of the bankrupt had been liquidated. *Id.* To the extent that *Papeleras* stands for the proposition that under section 304(c) the local creditor must enjoy equal status under the foreign law as it would in the United States, this Court respectfully disagrees and views it as another example of protectionism. However, to the extent that *Papeleras* stands for the proposition that a § 304 petitioner's request to turnover assets to a foreign forum will be denied where the laws of the foreign court do not comport with the Code's notion of fair and equal treatment of all creditors because claims are not recognized under Spanish law until liquidated, this Court is in agreement.

Therefore, this Court will next turn to the § 304(c) factors to determine whether, in light of the aforementioned objectives and concerns, comity should be granted and the funds turned over to the Petitioner to be administered in the Swiss proceeding.

Section 304(c)(1) calls for the just treatment of all holders of claims against or interest in the bankrupt's estate. The Swiss laws call for an orderly administration of the bankrupt estate. Refco concedes that Swiss law does not discriminate against non-Swiss creditors. As stated above, this Court rejects Refco's argument that in order to find just treatment, Refco's claim must be treated the same under Swiss law as under American and New York law.

Section 304(c)(2) goes to the inconvenience and prejudice of the local creditor if required to participate in the foreign proceeding. This calls for a balancing between the inherent prejudice and inconvenience to local creditors if required to participate in proceedings abroad against the economic and expeditious administration of the foreign bankrupt's estate.

When a United States creditor conducts business with a foreign corporation, the ever present risk is that the creditor will be forced to adjudicate its claim against the foreign corporation in the foreign country. Courts have recognized the implied assumption of this risk by U.S. creditors:

> [E]very person who deals with a foreign corporation impliedly subjects himself to such laws of the foreign government, affecting the powers and obligations of the corporation with which he voluntarily contracts, as the known and established policy of that government authorizes. To all intents and purposes, he submits his contract with the corporation to such a policy of the foreign government, and whatever is done by that government in furtherance of that policy, which binds those in like situation with himself, who are subjects of the government, in respect to the operation and effect of their contracts with the corporation, will necessarily bind him. He is conclusively presumed to have contracted with a view to such laws of that government, because the corporation must of necessity be controlled by them, and it has no power to contract with a view to any other laws with which they are not in entire harmony. It follows, therefore, that anything done at the legal home of the corporation, under the authority of such laws, which discharges it from liability there, discharges it everywhere."

Canada Southern Railway v. Gebhard, 109 U.S. 527, 537-38, 3 S.Ct. 363, 370, 27 L.Ed. 1020 (1883) (quoted in *Matter of Culmer*, 25 B.R. at 632).

Refco, as a sophisticated creditor with substantial assets and European offices, must have contemplated the risks involved when it decided to conduct business with Mebco, a foreign business. Refco does not claim that it is unable to assert its claim in Switzerland, rather it seeks to maintain the same rights it enjoys under domestic laws. As the court in *Matter of Culmer* observed, "[o]ne who invests in a foreign corporation subjects his investment to foreign law and may not seek to obtain greater rights than his co-creditors by

suing in an American court." *Culmer*, 25 B.R. at 632. Any prejudice and inconvenience to Refco in being forced to assert its claim in Switzerland is nothing more than what it should have understood to be a possible outcome of conducting business with Mebco. Certainly, a fair, economical and expeditious administration of Mebco's estate should not be jeopardized simply because Refco is not pleased with the results of its assumption of certain risks.

Section 304(c)(3) is satisfied insofar as Swiss law provides for setting aside preferential or fraudulent dispositions of property.

Section 304(c)(4) provides that distribution under the Swiss laws be in substantial accordance with the provisions of the Code. Refco does not dispute that Switzerland's insolvency procedures are fundamentally fair. In fact, they are substantially similar to ours. Once a bank is placed into liquidation, the Federal Banking Commission appoints a liquidator to administer the bank's assets and to act for the bank in all areas. If the bank is found to be insolvent, the assets are distributed pursuant to Swiss law. Creditors have the right to petition the Swiss court if they are dissatisfied with their distribution. Just like the Code, Swiss law provides for a ranking of creditors and for equal treatment of creditors within the same ranking. Again, section 304(c)(4) calls for *substantial accordance* with, not *absolute accordance* with, the provisions of the Code. The fact that Refco's claim enjoys different status under Switzerland's laws does not show that there is not substantial similarity. Moreover, the factor goes to the procedural fairness and due process of the foreign laws.

A consideration of the § 304(c) factors leads this Court to conclude that comity should be granted to the Swiss bankruptcy proceedings. The laws of Switzerland are not repugnant and violative of our fundamental notions of fairness. As with the bankruptcy cases in this country, the marshalling of Mebco's assets should be conducted in one forum with one set of laws so as to ensure equality among all of the creditors. The concerns raised by Refco are not sufficiently compelling to deny comity and allow the attached funds to be

enjoyed by Refco at the expense of all of Mebco's other creditors. Therefore, the funds in Mebco's bank account in Swiss Bank are hereby directed to be turned over to the Petitioner as Official Liquidator of Mebco.

Petitioner's Claim for Wrongful Attachment

The Petitioner seeks damages for wrongful attachment. Petitioner argues that attachment was obtained wrongfully because Refco was aware, prior to the time it went to the district court, that the Swiss insolvency proceedings had commenced and that Refco was required to seek relief in Switzerland. However, absent a ruling by a court of competent jurisdiction directing Refco to litigate its claims in Switzerland, Refco was fully entitled to pursue its remedies under American law. Therefore, the Petitioner's claim for damages is denied.

Summary Judgment

Rule 56(c) of the Federal Rules of Civil Procedure, made applicable to bankruptcy adversary proceedings by Bankruptcy Rule 7056, provides that summary judgment should be granted "if the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(c). As the Supreme Court held in *Celotex Corp. v. Catrett*, 477 U.S. 317, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986), the standard for ruling on a summary judgment motion is similar to that of a directed verdict if under governing law there can be but one reasonable conclusion. In addition the Supreme Court noted, in *Anderson v. Liberty Lobby Inc.*, 477 U.S. 242, 247-48, 106 S.Ct. 2505, 2510, 91 L.Ed.2d 202 (1986), that "the mere existence of some alleged factual dispute between the parties will not defeat an otherwise properly supported motion for summary judgment; the requirement is that there be no genuine issue as to any material fact." *Id.* Accordingly, material facts have been defined as those whose resolution will be

determinative of the outcome. *See also Pererira v. Hong Kong & Shanghai Banking Corp. (In re Kam Kuo Seafood Corp.)*, 76 B.R. 297, 300 (Bankr. S.D.N.Y. 1987).

An examination of the motion papers and accompanying documents before this Court indicates that no genuine dispute exists as to any material facts stated in the parties' respective local rule 13(h) statements. Rather the facts asserted by the parties are substantially similar. To the extent that there are facts in dispute, summary judgment is not defeated because these disputes do not represent "material issues of fact." *Id.* at 300. *Accord Shaw v. Jamaica Savings Bank (In re Cohen)*, 63 B.R. 104, 106 (Bankr. E.D.N.Y. 1986).

CONCLUSION

Accordingly, the Petitioner's motion for summary judgment is granted and Refco's cross-motion for summary judgment is denied. The funds in the Swiss Bank - N.Y. account are ordered to be turned over to the Petitioner for the purpose of administering the funds pursuant to the Swiss liquidation proceedings. The Petitioner's claim for damages is denied for failure to show cause for such relief. Also, the balance of the Petitioner's requests in its motion are denied in light of this Court's decision to turnover the funds.

The Petitioner is hereby directed to settle an order on five (5) days notice.

DATED: New York, New York
August 23, 1991

UNITED STATES BANKRUPTCY JUDGE

Date of Entry: August 26, 1991

Presentment Date;
September 4, 1991
12:00 o'clock noon

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

Case No. 90-B-10037 (CB)

In Re:

KOREAG, CONTROLE et REVISION S.A., as Official Liquidator of MEBCO BANK, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

ORDER GRANTING SUMMARY JUDGMENT ON A PETITION UNDER 11 U.S.C. § 304

Upon the Summons and Petition; Petitioner's motion for summary judgment on the Petition, and supporting papers; Refco F/X Associates, Inc.'s ("Refco") cross-motion for summary judgment dismissing the Petition, and supporting papers; the Answer of Party in Interest Osuuspankkien Keskuspankki Oy, and related papers; the Answer, Objections and Application for Relief of Party in Interest Barakat Diab, and related papers; all other proceedings and submissions herein; oral argument having been had and the Court having issued its Decision dated August 23, 1991; and good cause appearing therefor, it is hereby

ORDERED, that Petitioner's motion for summary judgment on the Petition is granted, except that Petitioner's claim for damages for wrongful attachment is denied, and Refco's cross-motion for summary judgment is denied; and it is further

ORDERED, that Refco is permanently enjoined from continuing the action it began against Mebco Bank, S.A. ("Mebco") in the District Court, styled *Refco F/X Associates, Inc.* v. *Mebco Bank, S.A.*, 89 Civ. 3071 (WK) (S.D.N.Y.), and it is further

ORDERED, that Swiss Bank Corporation is directed immediately to turn over all of the funds held in Mebco's account at Swiss Bank Corporation New York branch to the Petitioner for the purpose of administering these funds pursuant to the Swiss insolvency proceedings.

Dated: New York, New York
September 4, 1991

So Ordered:

_____

UNITED STATES BANKRUPTCY JUDGE

Date of Entry: September 4, 1991

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
91 Civ. 6212 (WK)

In Re:

KOREAG, CONTROLE et REVISION S.A., as Official Liquidator of MEBCO BANK, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

MEMORANDUM AND ORDER

WHITMAN KNAPP, D.J.

Petitioner having appealed from the final Order and Judgment of the Bankruptcy Court (Blackshear, Bankruptcy Judge) entered on September 4, 1991; and we having considered the briefs and oral statements of the parties in support of and in opposition to such appeal, it is ordered and adjudged that such Order and Judgment be affirmed on Judge Blackshear's opinion below.

The Petitioner having moved for a stay of enforcement of the said Order and Judgment pending an appeal to the Court of Appeals from this Order of Affirmance, such petition is granted to the extent of staying the enforcement of said Order and Judgment until September 30, 1991 at 5:00 p.m. to permit the petitioner to apply to the Court of Appeals for a further stay, but it is otherwise denied. The Court of Appeals may, of course, at any time either further extend this stay or vacate this order granting it.

SO ORDERED.

New York, New York
September 13, 1991

WHITMAN KNAPP, U.S.D.J.

Date of Entry: September 13, 1991

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

91 Civ. 6212 (WK)

In re

KOREAG, CONTROLE et REVISION, S.A. as Official Liquidator of MEBCO BANK, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

REVISED MEMORANDUM AND ORDER

WHITMAN KNAPP, D.J.

Refco F/X Associates ("Refco") having appealed from the final Order and Judgment of the Bankruptcy Court (Blackshear, Bankruptcy Judge) entered on September 4, 1991; and we having considered the briefs and oral statements of the parties in support of and in opposition to such appeal, it is ordered and adjudged that such Order and Judgment be affirmed on Judge Blackshear's opinion below.

Refco having moved for a stay of enforcement of the said Order and Judgment pending an appeal to the Court of Appeals from this Order of Affirmance, such motion is granted to the extent of staying the enforcement of said Order and Judgment until September 30, 1991 at 5:00 p.m. to permit Refco to apply to the Court of Appeals for a further stay, but it is otherwise denied. The Court of Appeals may, of course, at any time either further extend this stay or vacate this order granting it.

SO ORDERED.

New York, New York
September 16, 1991

WHITMAN KNAPP, U.S.D.J.

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New York, New York 10105

Date of Entry: September 16, 1991

Accepting the annexed letter from Refco F/X Associates as a motion to reconsider our Memorandum and Order of September 13, 1991, it is granted to the extent of replacing the designation of "petitioner" with the words "Refco F/X Associates" ("Refco"), and it is otherwise denied. A revised Memorandum and Order, a copy of which is attached hereto, is simultaneously being filed. The third paragraph of Refco's letter suggests that it had in some way been prejudiced because its arguments before us were directed only to its "Motion for a Stay Pending Appeal" rather than to the "merits" of the appeal itself. We find this suggestion to be frivolous. Refco's basis for seeking a stay was its contention that the appeal would become moot unless a stay were granted. In such circumstances it is frivolous to suggest that Refco would have held back any available arguments that could have supported its contention that "There is a Substantial Possibility that Refco Will Prevail on Appeal," Refco Mem. at 9.

SO ORDERED.

DATED: September 16 1991
New York, New York

WHITMAN KNAPP, U.S.D.J.

Date of Entry: September 16, 1991

A-447
MEMO ENDORSED

[LETTERHEAD OF GRAUBARD MOLLEN HOROWITZ POMERANZ & SHAPIRO]

September 13, 1991

BY HAND

Honorable Whitman Knapp
United States District Judge
Southern District of New York
40 Centre Street - Room 1201
Foley Square
New York, New York 10007

Re: In re Koreag, Controle et
Revision, S.A.
91 Civ. 6212 (WK)

Dear Judge Knapp:

We are constrained to call your Honor's attention to two inaccuracies contained in your Memorandum and Order dated earlier today.

The first and second paragraphs of the Memorandum and Order refer to the appellant and movant for a stay as the "Petitioner." Refco F/X Associates, Inc. ("Refco") is the appellant and was the party that moved for a stay pending appeal. Petitioner opposed Refco's motion.

Also, your Memorandum and Order states that the Court considered "the briefs and oral statements of the parties in support of and in opposition to such appeal. . . ." However, the briefs submitted and oral statements made to your Honor were directed only to Refco's motion for a stay pending appeal. There was no oral argument on the merits of the appeal. Nor was our brief a full brief in support of the merits on Refco's appeal.

MEMO ENDORSED

Copies Mailed to Counsel of Record E.H.

Accordingly, we respectfully request that the Memorandum and Order be corrected.

Respectfully submitted,

Jack Weinberg

/clm

cc: Celia Goldwag Barenholtz, Esq.
Kronish, Lieb, Weiner & Hellman - (Via Telecopier)
Paula Desel, Esq.
Arnold & Porter - (Via Telecopier)

Supreme Court, U.S.
FILED
AUG 5 1992
OFFICE OF THE CLERK

(2)

No. 92-87

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

In re: KOREAG, CONTROLE et REVISION, S.A., as Official Liquidator of Mebco Bank, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

KOREAG, CONTROLE et REVISION, S.A.,

Petitioner,

v.

REFCO F/X ASSOCIATES, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION

JACK WEINBERG
(Counsel of Record)
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QUESTIONS PRESENTED

1. Whether the Second Circuit was correct to (a) interpret Bankruptcy Code § 304(b)(2) in accordance with its plain language, as requiring a court first to determine an adverse party's good faith claim of ownership of property, because the plain language of § 304(b)(2) expressly limits the court's power to turnover property to a foreign representative of a foreign debtor's estate to "property *of* such estate," and (b) reject petitioner's attempt to rewrite § 304(b)(2), so as to avoid a determination of ownership, by replacing the turnover words, "property *of* such estate," with the words "property *involved in* such foreign proceeding," which appear in another subsection of the statute and set the standard for granting injunctive relief to the foreign representative.

2. Whether the Second Circuit correctly applied the well-established choice of law rules to the particular facts of this case, in holding that ownership of the specific property at issue here should be decided under New York law, rather than under Swiss Law.

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Refco is *not*, as the Liquidator would have this Court believe, a creditor seeking unfairly to gain priority over other similarly situated creditors. 2

The pertinent facts showing that the property in dispute belongs to Refco are set forth in the Second Circuit's decision. 3

The bankruptcy and district courts below failed to read § 304(b)(2) in accordance with its plain language and, as a consequence, ordered a turnover of Refco's property to the Liquidator. 4

The Second Circuit reversed the lower courts and held that the plain language of § 304(b)(2) required the bankruptcy court to determine Refco's claim of ownership of the property and that, under the facts here, the issue should be decided under New York law. 5

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RESPONDENT'S BRIEF IN OPPOSITION

Respondent, Refco F/X Associates, Inc. ("Refco"), respectfully submits that the petition for a writ of *certiorari* to the Court of Appeals for the Second Circuit, filed by the foreign liquidator (the "Liquidator") of a defunct bank being liquidated in Switzerland ("Mebco"), should be denied.[1]

This case presents no issue requiring Supreme Court review. The Second Circuit's decision interpreting Bankruptcy Code § 304(b)(2), 11 U.S.C. (1988), ("§ 304(b)(2)") applied, and is consistent with, this Court's repeated pronouncements that unambiguous language of a statute is to be interpreted in accordance with its plain meaning. The Second Circuit also followed well-settled choice of law rules and, based on the subject property's location in New York and the parties' substantial activities in New York, concluded that New York has a greater interest in the property dispute here than does Switzerland. The Second Circuit's decision is consistent also with this Court's holdings that, whereas bankruptcy law defines a debtor's estate generically, other applicable law that governs individual property rights absent bankruptcy determines whether the debtor or an adverse claimant has a greater interest in the specific property at issue, so as to prevent a debtor from forum shopping or receiving a windfall merely by reason of the happenstance of bankruptcy.

The Second Circuit decision is not in conflict with any decision of another court of appeals on the same matter. Nor did the Second Circuit decide a federal question in a way that conflicts with a state court of last resort. Nor does this case involve an important question of federal law which should be settled by this Court. The Second Circuit's decision is likely to have limited impact because it will affect few potential litigants.

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[1] Refco has no subsidiary companies. Its parent is Refco Group Ltd.

COUNTERSTATEMENT OF THE CASE

Congress stated clearly the standard for granting turnover of property to a foreign representative under § 304(b)(2). § 304(b)(2) provides that a court may turnover to a foreign representative of a foreign debtor's estate "the property *of* such estate, or the proceeds *of* such property . . ." (emphasis added). The prefatory clauses of § 304(b) provide that a foreign representative's turnover petition may be "controverted" by "a party in interest," including at "trial."[2]

Refco is *not*, as the Liquidator would have this Court believe, a creditor seeking unfairly to gain priority over other similarly situated creditors. Refco claims ownership of the *specific* property at issue and opposes the Liquidator's attempt to obtain a turnover of Refco's property so as to inflate the foreign debtor's estate. In distinguishing the unique facts of this case, the Second Circuit noted that Refco is not a prebankruptcy creditor that, without any ownership interest in specific assets claimed by the foreign debtor, rushed into a United States court to obtain an attachment of *any* property in an effort to improve its position at the expense of similarly situated creditors.

The Liquidator invoked § 304(b)(2) to obtain a turnover of approximately $11 million (the "Fund"), which is being held by the New York agent bank of the foreign debtor, Mebco. The Fund belongs to Refco. It represents currencies that Refco delivered *after* Mebco was put into liquidation and *after* the Liquidator was appointed. Refco delivered its currencies pursuant to prior agreements with Mebco *simultaneously* to exchange U.S. and foreign currencies. Refco performed its side of the agreements in the mistaken belief that Mebco was ready and able to perform, and without knowing that Mebco was put into liquidation between the time that the agreements were made and the time that the parties were to perform their simultaneous exchanges.

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[2] "Trial" means a trial on the merits. 124 Cong. Rec. 32,394 (1978).

Upon learning of Mebco's liquidation and non-performance of its side of the exchange agreements, Refco timely and properly exercised its rights under New York law to recover the Fund. Refco also commenced an action in New York federal court for the return of its money and a declaration that Mebco's agent bank is holding the Fund in constructive trust for Refco. Refco attached the Fund to insure its return.

The pertinent facts showing that the property in dispute belongs to Refco are set forth in the Second Circuit's decision. During the period from April 20, 1989, to 9:00 A.M. (EST) on April 27, 1989, Refco and Mebco entered into several agreements *simultaneously* to purchase currencies from, and sell currencies to, one another. Refco was to receive U.S. dollars from Mebco in exchange for foreign currencies, and Refco was to receive foreign currencies from Mebco in exchange for U.S. dollars. The agreed dates for these exchanges were April 27, 28, and May 2, 1989. The agreements were to be performed through Refco's New York office, with Citibank, N.A. ("Citibank"), in New York, acting for Refco. Mebco agreed that its deliveries and receipts of U.S. dollars would be transacted through Mebco's unaffiliated New York agent bank ("Swiss Bank-N.Y.").

On April 27, 1989, at 10:15 A.M. (EST), immediately after Refco and Mebco entered into the agreements, Swiss banking authorities placed Mebco into liquidation. Some forty-five minutes later, the authorities appointed the Liquidator. Later that day, Mebco's agent, Swiss Bank-N.Y., stopped all payments *out* of Mebco's account, but thereafter accepted transfers by Refco *into* Mebco's account.

Refco was not informed, and did not know, of Mebco's liquidation. Neither Mebco, nor the Liquidator, nor Swiss Bank-N.Y. informed Refco that (a) Mebco's financial condition had severely deteriorated from that which Mebco previously had represented to Refco, (b) Mebco was in liquidation, (c) Mebco would not perform its side of the simultaneous exchange agreements, or (d) Mebco's Swiss Bank-N.Y. account

remained open after liquidation to receive Refco's funds, but was frozen for payment of funds.[3]

Refco performed its side of the agreements after Mebco's liquidation began. From 3:46 P.M. (EST), on April 27, 1989, to May 2, 1989, Refco's New York bank delivered U.S. dollars to Mebco through Swiss Bank-N.Y., and foreign currencies to Mebco's accounts at banks abroad. But, unbeknownst to Refco at the time, Mebco failed simultaneously to deliver to Refco's Citibank accounts foreign currencies against U.S. dollars that Refco delivered to Swiss Bank-N.Y., or the U.S. dollars at Swiss Bank-N.Y. that were to have been delivered against Refco's transfer of foreign currencies.

On May 3, 1989, having learned that Mebco had not performed its side of the simultaneous currency exchanges, Refco called Mebco to ascertain why. Refco was told that Mebco's banking license had been revoked and that the Liquidator had been appointed. Refco thereupon demanded the immediate return of the currencies that Refco delivered as its part of the transactions that Mebco had not performed. Mebco and the Liquidator, however, failed and refused either to perform Mebco's side of the transactions or to return Refco's money. The total at issue is the Fund of approximately $11 million, plus interest, being held by Swiss Bank-N.Y.

The bankruptcy and district courts below failed to read § 304(b)(2) in accordance with its plain language and, as a consequence, ordered a turnover of Refco's property to the Liquidator. On May 5, 1989, Refco commenced an action against Mebco in the United States District Court for the Southern District of New York to recover the Fund and attached the Fund at Swiss Bank-N.Y. The Liquidator moved to dismiss Refco's complaint on the grounds of *forum non conveniens* and comity, so that Refco's money could be distributed to Mebco's creditors in Switzerland. The district

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[3] The statement in the Liquidator's petition for *certiorari*, that Refco performed "after the public announcement of Mebco's liquidation" (Pet. at 8), is misleading. The parties stipulated below that Refco does not subscribe to the newswire service that reported Mebco's liquidation.

court found that the parties and their performance of the agreements at issue had a substantial New York nexus, and denied the Liquidator's motion to dismiss for *forum non conveniens*. The court concluded that the question of ownership of the Fund should be decided in a § 304 turnover case and gave the Liquidator leave to bring such a case. 108 B.R. 29, 31 (S.D.N.Y. 1989).

In January 1990, the Liquidator filed a § 304 petition in the bankruptcy court for turnover of the Fund. Refco moved to dismiss the petition on the ground that the Fund belongs to Refco. Refco asserted that, since § 304(b)(2) expressly limits turnover to "property of" the foreign debtor's estate, the court could not turnover Refco's money to the Liquidator. The Liquidator moved for summary judgment, contending that (a) the words "property of such estate" in § 304(b)(2), which set the turnover standard, should be read as "property involved in such foreign proceeding," which is a clause in § 304(b)(1)(A)(i) that sets the injunctive relief standard, and (b) the Fund somehow is "involved in" Mebco's foreign proceeding. Refco filed a cross-motion for summary judgment based on the plain language of § 304(b)(2). Refco also disputed the Liquidator's assertion that the Fund is property "involved in" the Swiss proceeding.

The bankruptcy court rejected Refco's contention that, under § 304(b)(2), it should make a threshold determination of ownership of the Fund. 130 B.R. 705, 711 (Bankr. S.D.N.Y. 1991). The court refused to distinguish between the different standards that Congress set for turnover, in § 304(b)(2), and injunctive relief, in § 304(b)(1)(A)(i), and applied the injunctive relief standard to the turnover issue. The bankruptcy court held that, under Swiss law, Refco's Fund at Swiss Bank-N.Y. is "included in the property *involved in* Mebco's liquidation proceedings" and should be turned over to the Liquidator for disposition in the foreign liquidation proceeding. 130 B.R. at 712 (emphasis added). The bankruptcy court order was affirmed summarily by the district court, on the "opinion below." Pet. App. at 70a.

The Second Circuit reversed the lower courts and held that the plain language of § 304(b)(2) required the

bankruptcy court to determine Refco's claim of ownership of the property and that, under the facts here, the issue should be decided under New York law. The Second Circuit held that the clause allowing "turnover of the property of" the foreign debtor's estate requires that where, as here, "an adverse claimant raises a plausible dispute concerning the ownership of property whose turnover is sought by a foreign liquidator pursuant to § 304(b)(2), a court should resolve that threshold issue before ordering turnover." 961 F.2d 341, 348 (2d Cir. 1992). The court reasoned that "the use of the term 'property of such estate' presupposes an antecedent determination of property interests as a condition to the turnover of property to a foreign representative." *Id.*

The Second Circuit held that, for purposes of § 304, while the law of the jurisdiction in which the foreign proceeding is pending defines the *types* of property that comprise the foreign debtor's estate, other applicable law governing individual property rights absent bankruptcy determines whether the *particular* property at issue belongs to the debtor's estate or to an adverse claimant. 961 F.2d at 348.

In deciding whether the ownership dispute should be resolved under New York law or Swiss law, the Second Circuit reviewed the New York and Swiss contacts of the dispute and found that New York had the more significant contacts and, therefore, the greater interest in the dispute. Based on well-settled choice of law rules, the court held that New York law governs. *Id.* at 350-51.

REASONS FOR DENYING *CERTIORARI*

No other court of appeals has interpreted § 304(b)(2) and the Second Circuit decision does not depart from well-established law. The court reached the correct and fair result (a) by following this Court's repeated pronouncements that (i) statutory language must be construed in accordance with its plain meaning, and (ii) rights to specific disputed property should be determined by the law that governs absent bankruptcy, so that a debtor will not receive a windfall merely by reason of the happenstance of bankruptcy, and (b) by applying

well-settled choice of law rules to the particular facts of this case.

It is unlikely that a case such as this will arise again. It is doubtful that other foreign representatives will follow the lead of the Liquidator here and attempt to obtain a turnover of property known to belong to someone else.

1. This Court Should Not Grant *Certiorari* To Review The Second Circuit's Interpretation of § 304(b)(2) In Accordance With Its Plain Meaning.

§ 304(b)(2) provides that:

> [I]f a party in interest does not timely controvert the petition, or after trial, the court may - . . . (2) order turnover of the *property of such estate*, or the proceeds of such property, to such foreign representative; . . .

(emphasis added).

The Second Circuit held that the statutory language of § 304(b)(2) -- "property of such estate" -- limits a court's turnover power to property that belongs to the foreign debtor's estate. 961 F.2d at 348 ("[t]his interpretation of § 304(b)(2) is supported by the language of the statute"). Based on the statute's plain language, the court concluded that, where, as here, "an adverse claimant raises a plausible dispute concerning the ownership of property whose turnover is sought by a foreign liquidator pursuant to § 304(b)(2), a court should resolve that threshold issue before ordering turnover." *Id.*

The Second Circuit rejected the Liquidator's argument that § 304(b)(2) should be rewritten by replacing its words "property *of* such estate," relating to turnover, with the § 304(b)(1) words "property *involved in* such foreign proceeding," relating to injunctive relief. *Id.* at 349 (emphasis added). The court contrasted the turnover language of § 304(b)(2) with the injunctive relief language of § 304(b)(1):

> While § 304(b)(1) empowers a bankruptcy court to enjoin litigation "with respect to property involved in" a foreign insolvency proceeding, presumably "to

> prevent dismemberment by local creditors of assets located here," S. Rep. No. 989 at 35, § 304(b)(2) authorizes turnover only of "property of such estate, or proceeds of such property." *Thus, the use of the term "property of such estate" presupposes an antecedent determination of property interests as a condition to the turnover of property to a foreign representative.*

Id. at 348 (emphasis added). The court concluded that "Congress used different language" in the two subsections "and we are not at liberty to ignore this legislative choice." *Id.* at 349.

The Second Circuit's decision adheres to the fundamental tenet of statutory construction that statutory language is to be interpreted in accordance with its plain meaning. This Court has applied this principle of statutory construction to the Bankruptcy Code. *See, e.g., Patterson v. Shumate,* 112 S. Ct. 2242, 2246 (1992) ("the plain language of the Bankruptcy Code and ERISA is our determinant"); *United States v. Ron Pair Enter., Inc.*, 489 U.S. 235, 241 (1989) ("the sole function of the courts is to enforce [a statute] according to its terms"). This Court recently reiterated this principle unequivocally and without dissent: "[w]e have stated time and again that courts must presume that a legislature says in a statute what it means and means in a statute what it says there. When the words of a statute are unambiguous, then, this first canon is also the last: 'judicial inquiry is complete'." *Connecticut Nat'l Bank v. Germain*, 112 S. Ct. 1146, 1149 (1992) (citations omitted).

Here, the statutory provisions that allow "a party in interest" to "controvert" a turnover petition and a court to "order turnover of the property of such estate" are clear and unambiguous statements by Congress that a court may order turnover only of property that belongs to the foreign debtor's estate, but not property that belongs to an adverse party.

The Second Circuit rejected the Liquidator's contention that property should be turned over under § 304(b)(2) so long as it fits within one of the *types* of property that assertedly comprise a debtor's estate under Swiss law:

> The applicable distinction is drawn in Lawrence P. King, 2 *Collier on Bankruptcy* ¶ 304.01, at 304-3 (15th ed. 1992) (emphasis added): "For purposes of section 304, the estate of a foreign debtor is defined by the law of the jurisdiction in which the foreign proceeding is pending, *with other applicable law serving to define the estate's interest in particular property.*" *See also In re Lines*, 81 B.R. 267, 271 (Bankr. S.D.N.Y. 1988) (same).

961 F.2d at 348 (emphasis in original). The decision follows this Court's pronouncements that, whereas bankruptcy law defines an estate generically, other applicable law that governs individual property rights absent bankruptcy determines whether a debtor or an adverse party has a greater right to the specific property at issue, so as "to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving 'a windfall merely by reason of the happenstance of bankruptcy.'" *Butner v. United States*, 440 U.S. 48, 55 (1979); *see also Barnhill v. Johnson*, 112 S. Ct. 1386, 1389 (1992) ("[i]n the absence of any controlling federal law, 'property' and 'interests in property' are creatures of state law").[4]

The Second Circuit disagreed with the Liquidator's argument that the court should turnover the Fund in dispute so that ownership could be determined in Mebco's Swiss liquidation proceeding:

> The power of the court extends to "property of [the] estate." § 304(b)(2). Once a plausible challenge is presented as to whether particular property falls within the statutory definition, the bankruptcy court whose authority is invoked must determine the legitimacy of that invocation. The nature of this determination demands that it be made prior to the turnover of the property. *It is unsatisfactory to say*

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[4] The Second Circuit's decision is consistent also with the holding in *In re Garrott & Sons*, 772 F.2d 462, 466 (8th Cir. 1985) (filing bankruptcy does not convert money held in debtor's bank account in constructive trust for another into property of the debtor's estate).

> *that the property should first be turned over, because it is the ascertainment that property is "of [the] estate" under local law that defines the extent of the court's power to issue the turnover order.*

961 F.2d at 349 (emphasis added).

Refco submits that, since the Second Circuit interpreted § 304(b)(2) in accordance with its plain language, the Liquidator's petition should be denied.

2. None Of The Liquidator's Arguments Supports A Departure From The Principle That § 304(b)(2) Is To Be Interpreted In Accordance With Its Plain Language.

The Liquidator's petition is premised on a mischaracterization of the Second Circuit's decision. The court did not hold that turnover under § 304(b)(2) "can only be granted as to assets which would be property of a domestic bankruptcy 'estate' under [Bankruptcy Code] § 541 . . ." (Pet. at 11, 14). To the contrary, the court stated clearly that, "'[f]or purposes of section 304, the estate of a foreign debtor is defined by the law of the jurisdiction in which the foreign proceeding is pending . . . .'" 961 F.2d at 348. The court held also that other applicable law that governs individual property rights absent bankruptcy determines whether the debtor's estate or an adverse party has a greater interest in the particular property at issue. *Id.* The court *thereafter* referred to § 541, 11 U.S.C. (1988 & Supp. II 1990), by way of "analogy" and as "further support" for the court's interpretation of the plain language of § 304(b)(2). 961 F.2d at 349. The court stated that, under § 541, "'[a]lthough federal bankruptcy law determines the outer boundary of what may constitute property of the estate, state law determines the 'nature of a debtor's interest' in a given item.'" *Id.* (citations omitted).

The Liquidator devotes a substantial part of its brief to rationalizing its assertion that the words "such estate" in § 304(b)(2) "can only be a short-hand reference to the original phrase 'property involved in such foreign proceeding' in 304(b)(1)(A)(i). . .," and that, therefore, both subsections 304(b)(2) and (b)(1)(A)(i) should be read as if they contain the phrase "property involved in such foreign proceeding," which

appears only in § 304(b)(1)(A)(i) (Pet. at 16). This argument completely ignores the limiting words "property *of*," which immediately precede the words "such estate" in § 304(b)(2), and overlooks the fact that Congress used the word "of" twice in § 304(b)(2) to modify and define the word "property:" "turnover of the property *of* such estate, or the proceeds *of* such property. . . ."

The suggested tortured parsing of § 304(b)(2) would require that the statutory word "of" be deleted from that subsection and replaced with the words "involved in," and that the words "such estate" be replaced by the words "such foreign proceeding." These proposed deletions and replacements of statutory provisions are impermissible. "[T]he settled rule [is] that a statute must, if possible, be construed in such fashion that every word has some operative effect." *United States v. Nordic Village, Inc.*, 112 S. Ct. 1011, 1015 (1992) (interpreting Bankruptcy Code § 106); *see also Freytag v. C.I.R.*, 111 S. Ct. 2631, 2638 (1991) (expressing "'a deep reluctance to interpret a statutory provision so as to render superfluous other provisions in the same enactment'").

Moreover, the attempt to ascribe the same meaning to the different limiting language used in the injunction provision of § 304(b)(1)(A)(i) and the turnover provision of § 304(b)(2) violates this Court's command that:

> "[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion." . . . "The short answer is that Congress did not write the statute that way." We refrain from concluding here that the differing language in the two subsections has the same meaning in each. We would not presume to ascribe this difference to a simple mistake in draftsmanship.

Russello v. United States, 464 U.S. 16, 23 (1983) (citations omitted). Here, too, had Congress intended to empower a bankruptcy court to order turnover of "property involved in the foreign debtor's proceeding," Congress would have expressly

done so. Instead, Congress chose to use that language only in the subsection relating to injunctive relief.

The Liquidator protests that it is illogical to hold that a court may issue injunctions, pursuant to § 304(b)(1), with respect to property "involved in" the foreign proceeding, without prior determination of ownership, but may not order turnover of property, pursuant to § 304(b)(2), unless the court first determines that it is "property of" the foreign debtor's estate (Pet. at 17-18). But, as the Second Circuit held: "Congress used different language in § 304(b)(1) and (2), the two provisions perform different functions, and we are not at liberty to ignore this legislative choice." 961 F.2d at 349. That the injunction provisions of § 304(b)(1) perform a different function is clear from (a) statements by bankruptcy courts that the provisions of § 304(b)(1) make available in a § 304 case the same stay that is available in domestic bankruptcy cases by virtue of Bankruptcy Code § 362, 11 U.S.C. (1988 & Supp. II 1990) (*see, e.g., In re Kingscroft Ins. Co., Ltd.*, 138 B.R. 121, 126 (Bankr. S.D. Fla. 1992); *In re Banco Nacional de Obras Y Servicios Publicos, S.N.C.*, 91 B.R. 661, 664 (Bankr. S.D.N.Y. 1988)), and (b) this Court's holding that a preliminary injunction preserves the status quo until a trial on the merits and "a party thus is not required to prove his case in full at a preliminary-injunction hearing" (*University of Texas v. Camenisch*, 451 U.S. 390, 395 (1981)).[5]

The Liquidator's arguments based on legislative history fail to satisfy its "'exceptionally heavy' burden of persua[sion]" that Congress did not intend § 304(b)(2) to be read in accordance with its plain meaning. *See Patterson*, 112 S. Ct. at 2248. The scant legislative history of § 304, to which the Liquidator refers (Pet. at 14), was considered by the Second Circuit (961 F.2d at 348) and does not address the plain words of § 304(b)(2) which limit turnover to property belonging to the foreign debtor's estate. The Liquidator's reliance on the

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[5] It is farfetched, at best, for the Liquidator to suggest (Pet. at 17-18) that a court would deny turnover to a foreign representative because the property belongs to an adverse claimant, and would permanently enjoin the adverse claimant from taking steps to recover its property.

legislative history of Bankruptcy Code § 306, 11 U.S.C. (1988), to interpret § 304 (Pet. at 17), is equally frivolous. § 306 is a "[l]imited appearance" statute which provides that filing a § 304 petition does not subject the foreign representative to jurisdiction for purposes *other than* determinations of disputes under § 304.

In an attempt to write § 304(b)(2) out of the statute, the Liquidator argues that the central focus of § 304 is comity, which is mentioned in § 304(c)(5), and that the only real issue for a bankruptcy court on a turnover petition is under § 305(c), *i.e.*, whether "American creditors will receive due process in the foreign tribunal" (Pet. at 13, 18). That argument, however, totally ignores the fact that Congress chose to put in § 304(b) the right of a "party in interest" to "controvert the petition," including at "trial." The plain language of § 304(b) shows that a court may not consider any of the factors in § 304(c), including comity, unless it has determined that the conditions of § 304(b) have been satisfied. Only if the court determines that the conditions of § 304(b) have been satisfied, and therefore the relief provided therein is *available*, may the court apply the § 304(c) criteria to determine whether it is *appropriate* to grant the relief requested.

Furthermore, the legislative history shows that comity was added as one of the six factors listed in § 304(c) to make clear that comity is to be considered "in addition to the other factors. . . ." 124 Cong. Rec. 32,394 (1978). As one commentary put it: "Comity is not shorthand for turnover." Morales and Deutsch, *Bankruptcy Code Section 304 and U.S. Recognition of Foreign Bankruptcies: The Tyranny of Comity*, 39 Bus. Law. 1573, 1594 (1989).

The Liquidator is being illogical in yet another respect. On the one hand, it recognizes that on a § 304 turnover petition a bankruptcy court must hold a hearing to determine whether the criteria set forth in § 304(c) have been satisfied (Pet. at 18). On the other hand, the Liquidator contends that it would controvert the purpose of § 304 and be dilatory for the court to hear and determine whether the subject property actually belongs to the foreign debtor (Pet. at 11, 20 n.3). If the Second Circuit had accepted the Liquidator's proposition, it would have

led to the absurd result that disputed property would be turned over unquestioningly every time a foreign representative asserts that the property "is part of the property being administered abroad," without regard to who possesses or owns the property (Pet. at 18). The Liquidator illustrated the absurdity of its position at oral argument before the Second Circuit. The Liquidator was asked if funds stolen from Refco by a representative of Mebco and deposited in Mebco's account at Swiss Bank-N.Y. would be subject to turnover for disposition in Switzerland. The Liquidator answered "yes."

Also frivolous is the assertion that the Second Circuit decision will "complicate[ ] efforts of foreign representatives to marshall assets in a single forum . . ." (Pet. at 12). The Liquidator's right to marshall the foreign debtor's *assets* is not a license to grab property that belongs to someone else: "A determination that the funds are not property of the estate therefore does not improperly affect other creditors of the estate, because they have valid claims only against the estate's bona fide assets." 961 F.2d at 349. Nor will the Second Circuit's decision "reward fast moving domestic creditors" (Pet. at 11):

> [Refco's] position is that Mebco does not own the Disputed Funds. . . . The situation is clearly distinguishable from an effort by a normal bankruptcy creditor, without any plausible ownership claim to a specific asset, to gain a preferred position vis-a-vis other creditors by initiating a separate legal proceeding. *Cf. Victrix*, 825 F.2d at 714 (refusal to countenance attachment designed to evade writ of Swedish bankruptcy court); *Cunard*, 773 F.2d at 456 (same).

961 F.2d at 349-50.

The Liquidator's argument that *certiorari* should be granted because of an alleged "rising tide of transnational bankruptcies" (Pet. at 12) is rebutted by its own statistics. They show that an average of only fifteen § 304 petitions have been filed throughout the United States in each of the last five years. Moreover, the Liquidator does not argue that any of

these few petitions involved, as here, a party opposing turnover on the ground that it owns the property.

3. This Court Should Not Grant *Certiorari* To Review The Second Circuit's Factual Determination, Pursuant to Well-Settled Choice of Law Principles, That New York Law Decides Refco's Right To The Disputed Property.

The Second Circuit applied New York law to determine ownership of the Fund at issue based on the well-settled rule that the law of the jurisdiction having the greatest interest in the dispute will govern. *See Wells Fargo Asia Ltd. v. Citibank, N.A.*, 936 F.2d 723 (2d Cir. 1991), *cert. denied*, 120 L. Ed. 2d 868 (1992). The Liquidator acknowledges that the Second Circuit applied the correct conflicts rule, but contends that the particular facts of the case warrant the conclusion that Switzerland, rather than New York, has the greatest interest in the dispute over the Fund (Pet. at 20-21).

The Second Circuit's decision that "New York has a superior interest in the particular question at issue here" is fully supported by the record. 961 F.2d at 351. It shows that: The Fund is located in New York. Refco is a New York corporation with its principal place of business in New York. Refco performed its side of the currency exchange agreements in New York. Refco's confirmations of each of the transactions were prepared in, and sent to Mebco from, New York. Mebco agreed to pay U.S. currency to Refco, and to receive U.S. currency from Refco, through Swiss Bank-N.Y. Mebco so instructed Swiss Bank-N.Y. by telefacsimiles sent directly to Swiss Bank-N.Y. *Id.*

Furthermore, it is fundamental that the Supreme Court's judicial resources should not be exercised to review factual findings. *See New York Dock Co. v. S.S. Poznan*, 274 U.S. 117 (1927); *Boehmer v. Penn. R.R. Co.*, 252 U.S. 496 (1920).

CONCLUSION

For all the foregoing reasons, *certiorari* should be denied.

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August 5, 1992

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No. 92-87

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

In re:

KOREAG, CONTROLE ET REVISION, S.A. as Official Liquidator of MEBCO BANK, S.A. (In Liquidation) pursuant to the Insolvency Laws of the Federal Republic of Switzerland.

KOREAG, CONTROLE et REVISION, S.A.,

Petitioner,

—v.—

REFCO F/X ASSOCIATES, INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

SUPPLEMENTAL AND REPLY BRIEF

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FURTHER REASONS FOR GRANTING THE WRIT

I. This Case Should Be Reviewed

Refco's primary argument in opposition to the Liquidator's petition for certiorari is the contention that a case of this kind is unlikely to arise again because the Liquidator[1] is trying to obtain "turnover of property known to belong to someone else". Refco Br. at 7. But Refco is plain wrong when it asserts that the disputed property "belongs" to it. The disputed property consists of Mebco's bank account at Swiss Bank Corporation in New York. Contrary to the misleading impression created by Refco's brief, in addition to the monies paid into Mebco's account by Refco pursuant to various currency exchange agreements between Refco and Mebco, the account *also* contains millions of dollars paid in by others. All these funds have been commingled together, as is typical of any debtor's bank account. Thus, the "fund" which Refco repeatedly asserts "belongs" to it is in reality a bank account maintained by Mebco—clearly property of the foreign debtor.

As for the specific property interest alleged by Refco, Refco is asserting that as a result of Mebco's failure to perform certain currency exchange agreements entered into with Mebco before it was placed into liquidation, Refco is entitled to reclaim $5.3 million[2] of the monies in the account under the Uniform Commercial Code and have a constructive trust imposed on the remaining $5.7 million under state law. But the fact that Refco has formulated various legal theories which, if proved, would entitle it to obtain a judgment against Mebco, does not mean that the property "belongs" to Refco. The dis-

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1 The Liquidator has no subsidiaries. Its parent companies are listed in the Petition for Certiorari at ii.

2 While the Second Circuit understood the reclamation amount to be $6.9 million, the actual amount delivered by Refco to Mebco's bank account in New York for which there was no performance by Mebco was $5.3 million, as Refco acknowledged and as the district court held on July 30, 1992.

puted fund will "belong" to Refco only if the § 304 petition is denied, Refco proceeds to judgment in the breach of contract case it initiated in New York after the Swiss insolvency proceedings had begun and levies against Mebco's account pursuant to its ex parte attachment. Until that time, the funds in Mebco's New York bank account are part of the property being administered by the Liquidator for the benefit of all Mebco's creditors in Switzerland. In short, Refco's so-called ownership interest is simply the claim that it is owed money as a result of Mebco's insolvency and wants to be paid from Mebco's assets, a claim which could be made by all of Mebco's creditors.

Refco's claim that the property "belongs" to it is not only wrong as a matter of fact, it begs the question presented to this Court: does § 304 require that an American creditor's claim to an asset being administered in a foreign insolvency proceeding be adjudicated *before* that property may be turned over to a lawfully-appointed foreign representative under § 304? As set forth in the Liquidator's petition, § 304 is intended to be a forum selection device. Where, as here, an appellate court has determined that the bankruptcy court correctly found that the jurisdictional requirements of the statute have been met and properly balanced the 304(c) factors, all inquiry should be at an end. In holding that the bankruptcy court was required to go further and actually adjudicate the state law claims raised by a local creditor before granting turnover to a foreign representative, the Second Circuit undercut the whole reason for § 304—to have transnational bankruptcy proceedings administered in a single forum so that the claims of all creditors, foreign and domestic, can be equitably determined.

While Refco asserts that it is not an ordinary creditor seeking to take advantage of an ex parte attachment against a foreign debtor's American assets, it is impossible to describe what Refco has done any other way. The fund is not Refco's property; it is a bank account belonging to a foreign debtor against which any number of creditors could assert similar claims. Indeed, two other Mebco creditors have already attempted to

assert claims to part of the same fund which Refco seeks to seize. Under § 304, all these claims should be pursued in Switzerland so that equality of distribution, one of the prime tenets of our bankruptcy code, can be achieved.

This case presents precisely the situation § 304 was meant to address. A bank account belonging to a foreign debtor is just the kind of property one would expect a foreign debtor to have in the United States, especially if the foreign debtor is a bank. It is also the kind of property one would expect to be subject to distribution abroad. Indeed, far from being a unique situation, this case presents the exact scenario that caused Congress to enact § 304 in the first place. The impetus for § 304 came from the problems caused by the insolvencies of three foreign banks in the 1970's. Charles D. Booth, *Recognition of Foreign Bankruptcies: An Analysis and Critique of the Inconsistent Approaches of United States Courts*, The American Bankruptcy Law Journal 135, 143-46 (1992). Because this case should have been a routine application under §304, the precedent it sets will have grave consequences for the future use of § 304.

Refco's arguments about the "plain meaning" of Bankruptcy Code § 304 only underscore the need for this Court's review. Invoking the rule that, if possible, a statute must be construed to give every word "operative effect," Refco Br. at 11 (quoting *United States v. Nordic Village, Inc.*, 503 U.S. ____, 112 S. Ct. 1011, 117 L.Ed. 2d 181 (1992)), Refco relies on that part of the Second Circuit's opinion which quotes § 304 by deleting the term "such" estate and replacing the term "the" estate:

> The power of the court extends to "property of *[the]* estate." . . . It is unsatisfactory to say that the property should first be turned over, because it is the ascertainment that property is "of *[the]* estate" under local law that defines the extent of the court's power to issue the turnover order.

961 F.2d 341, 349 (emphasis added); *see also* Refco Br. at 9-10. The meaning of the statute can hardly be "plain" if a court

must change its terms to apply it: Erasing a term does not give it "operative effect".[3]

Refco's reliance on the Second Circuit's view that property "of such estate," *see* § 304(b)(2), cannot be property "involved in" the foreign proceeding, *see* § 304(b)(1), because 304(b)(2) and 304(b)(1) " 'perform different functions,' " Refco Br. at 12, is also inconsistent with the principle that the statute should be read as Congress wrote it. Section 304(b)(1), the injunctive arm of the statute, does not, in terms, limit the injunctive relief available to a foreign representative to a preliminary injunction. All the statute says is that the court may "enjoin the commencement or continuation of" certain actions. *See also* Charles D. Booth, *Recognition of Foreign Bankruptcies: An Analysis and Critique of the Inconsistent Approaches of United States Courts*, The American Bankruptcy Law Journal 135, 161 (1992) ("Section 304(b)(1) authorizes the bankruptcy court to enter interim or permanent relief"). Thus, on the Second Circuit's view, a bankruptcy court can permanently enjoin an action against funds involved in the foreign proceeding without a preliminary determination under state law that the money belongs to the foreign debtor but refuse to turn over the funds if it determines that the American creditor has a state-law right (rendered unenforceable by the injunction) to the funds.

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3 Nor does Refco's contention that the Second Circuit only invoked Bankruptcy Code § 541 as an analogy, rather than to define conclusively the property that could be turned over under § 304, obviate this Court's review. *See* Refco Br. at 10. The Second Circuit's opinion calls for evaluation of property interests under § 541 in § 304 proceedings. Indeed, Judge Blackshear, the Bankruptcy Judge presiding in this and other § 304 proceedings, apparently understood the Second Circuit's opinion this way. *See In re Laurencia Jaen Ocana*, Case No. 91-B-15233 (CB), Order Granting Preliminary Injunction under Section 304 in Case Ancillary to a Foreign Proceeding (Bankr. S.D.N.Y. June 8, 1992) (granting preliminary injunction in part because "Petitioner has met his burden of showing a probability of success on the merits under Bankruptcy Code Sections 304 and 541"). Only this Court's resolution of whether property rights under American law must be adjudicated in a § 304 proceeding will end confusion concerning the applicability of § 541 to § 304 petitions.

Refco also misreads that part of § 304(b) which states that a "party in interest" may "timely controvert the petition" and contemplating a "trial". Refco assumes that the basis upon which controversion is appropriate is ownership under American law of the assets subject to the 304 petition. Refco again begs the fundamental question whether a threshold determination of local creditors' claims under state law is necessary to resolve a 304 petition: The statute does not *say* that a bankruptcy court must hold a trial to decide who owns the local assets under American law, and the question presented to this Court is whether, despite the absence of an express requirement, a bankruptcy court must nevertheless hold a trial on that issue. Section 304's underlying purpose to avoid piecemeal distribution of assets in the United States dictates that the bankruptcy court adjudicate only the jurisdictional requirements of the statute and the relevant 304(c) factors. There is nothing in the statute's reference to a trial which even remotely suggests that the bankruptcy court must also adjudicate claims based on local law before ordering turnover. As two commentators put it:

> The statute contemplates final relief unless the petition is controverted or after resolution "at trial." "Controversion" is not defined. It has been accorded its dictionary meaning, deny or take issue with. The concept of "controversion" first involves the petitioner's standing. If there is a standing deficiency, the case should be dismissed. After standing is resolved (usually on documents), the court must consider whether the foreign proceeding qualifies for American judicial recognition and assistance under Section 304(c). Both standing and qualification may be challenged by a party at interest [sic]—the foreign debtor or the owners of or claimants to the local res. . . . A final Section 304 judgment should reserve all substantive issues to the foreign forum and its law once the standing and qualification standards have been met.

Brian J. Gallagher and John Hartje, *The Effectiveness of § 304 in Achieving Efficient and Economic Equity in Transnational*

Insolvency, 1983 Annual Survey of Bankruptcy Law 1, 8, 15 (1983)(footnotes omitted).

Finally, Refco attempts to portray the Liquidator's construction of § 304 as "absurd" by selectively quoting from the Liquidator's response to a question from the Second Circuit at oral argument. Refco Br. at 14. The panel asked counsel for the Liquidator whether stolen property could be subject to a turnover order. Counsel responded that if such property in question was part of the property being administered in Switzerland, and if the bankruptcy court determined that under those circumstances—quite different from those present here—the 304(c) factors still weighed in favor of ancillary relief, the bankruptcy court would have the power under 304 to order turnover. The Liquidator's answer was clearly correct. A determination that the 304(c) factors weigh in favor of relief is a finding that the foreign proceeding is fundamentally fair and equitable and should be afforded deference by our courts. Where such a finding has been made, it is inconsistent with the principle of comity and the plain language of 304 to deny turnover out of concern for the specific recovery a particular local creditor (the victim of theft, in the hypothetical posed by the Second Circuit) would receive abroad on its claim.

Commentators have long espoused the view of § 304 taken by the bankruptcy court and the district court in this action. Indeed, just prior to the Second Circuit's decision in this matter, Professor Charles D. Booth concluded an exhaustive treatment of § 304 with the apt observation that:

> It is time for U.S. bankruptcy judges, lawyers, and creditors to reject the territoriality approach and acknowledge that the U.S. does not have a monopoly over fair bankruptcy procedures. Many other countries have bankruptcy laws and procedures that, although differing in some respects from U.S. laws and procedures (such as by setting forth different priority rules or by requiring less creditor participation), are based on similar principles (the most important of which is the principle of equality of distribution), are just and fair in their overall treatment of

debtors and creditors, and are deserving of recognition by U.S. courts.

What John Lowell wrote a hundred years ago is just as appropriate today:

> It is obvious that, in the present state of commerce and of communication, it would be better in nine cases out of ten that all settlements of insolvent debtors with their creditors should be made in a single proceeding, and generally at a single place; better for the creditors, who would *thus share alike*, and better for the debtor, because all his creditors would be equally bound by his discharge.

Back in the 1880's, Lowell was forced to admit that "[i]t is not so easy to see how this result is to be reached in actual practice." Today, however, with the existence of § 304, not only has this result been reached in individual cases, but it is now possible to make this result the norm in cross-border insolvencies involving assets in the United States.

> . . . . Given the recent worldwide recession, many more § 304 cases will likely arise in the near future. The treatment by U.S. courts of these cases may well determine whether § 304 will survive in its present form or whether amendments will be necessary to achieve the worthwhile goal of increased cooperation in transnational insolvencies.

Charles D. Booth, *Recognition of Foreign Bankruptcies: An Analysis and Critique of the Inconsistent Approaches of United States Courts*, The American Bankruptcy Law Journal 135, 230, 232 (1992)(footnotes omitted) (quoting John Lowell, *Conflict of Laws as Applied to Assignments for Creditors*, 1 Harvard Law Review 259, 264 (1888) (emphasis added)); *See also* Brian J. Gallagher and John Hartje, *The Effectiveness of § 304 in Achieving Efficient and Economic Equity in Transnational Insolvency*, 1983 Annual Survey of Bankruptcy Law 1, 19 (1983) ("The proper role of a Section 304 case is the extension

of American equitable power to a foreign court in order to preserve the principle of equality economically achieved. . . . The only distribution expressly contemplated by the statute is a pourover of assets to a foreign court for eventual distribution there under qualifying foreign law").

II. This Case Is Ripe for Review

Since the Second Circuit's opinion, the lower courts in this matter have construed the Second Circuit to have mandated that judgment be entered for Refco on its claim for reclamation under the New York Uniform Commercial Code without a hearing. Specifically, on May 19, 1992, the bankruptcy court vacated the injunction it had imposed earlier on Refco's continuation of the action Refco had originally commenced in the district court (*Refco F/X Associates, Inc.* v. *Mebco Bank, S.A.*, 89 Civ. 3071 (WK)) with respect to Refco's reclamation claim, leaving Refco free to pursue its reclamation claim in district court. Refco then moved for summary judgment in the district court which was granted on collateral estoppel grounds. However, the district court has stayed execution of the judgment pending this Court's resolution of the petition for certiorari. Thus, as to $5.3 million (the amount the district court determined was reclaimable) of the funds in the account, the instant petition is clearly not interlocutory. Indeed, Refco has made no attempt to controvert the Liquidator's showing that this petition is ripe for review. Accordingly, there is no dispute that questions presented by this petition are in the proper posture to be reviewed by this Court.

CONCLUSION

The petition for certiorari should be granted.

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